

Internal Revenue bulletin

Bulletin No. 2003-26
June 30, 2003

HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Rev. Rul. 2003-66, page 1115.

Information reporting requirements. This ruling provides guidance to federal agencies about the information reporting requirements under sections 6041A and 6050M of the Code for the payment of services.

Rev. Rul. 2003-67, page 1119.

Obsolete revenue rulings. This ruling obsoletes prior rulings which have been identified as no longer being determinative.

Rev. Rul. 2003-68, page 1108.

LIFO; price indexes; department stores. The April 2003 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, April 30, 2003.

Rev. Rul. 2003-69, page 1118.

Small partnership exception. This ruling addresses the issue of whether a partnership qualifies for the small partnership exception provided in section 6231(a)(1)(B) of the Code, and thus does not fall within the unified audit and litigation procedures under sections 6221 through 6234 (TEFRA partnership provisions), where one of the partners is either an organization that is exempt from taxation under section 501(a) that meets the definition of a C corporation for federal tax purposes or a foreign corporation.

T.D. 9059, page 1109.

Final regulations under section 755 of the Code provide guidance to partnerships and their partners concerning the allocation of basis adjustments among partnership assets.

Notice 2003-37, page 1121.

This notice provides a proposed revenue procedure that establishes an optional procedure for payors who make payments in the course of their trade or business through payment cards to determine whether the payments are reportable under sections 6041 and 6041A of the Code.

Announcement 2003-40, page 1132.

This announcement describes changes the IRS is testing under section 32 of the Code in determining qualifying child eligibility under the Earned Income Credit.

ADMINISTRATIVE

T.D. 9060, page 1116.

REG-103809-03, page 1132.

Temporary and proposed regulations incorporate and clarify the phrase "return information reflected on returns" in conformance with the terms of section 6103(j)(5) of the Code. The temporary regulations also remove certain items of return information that the Department of Agriculture no longer needs for conducting the census of Agriculture.

(Continued on the next page)

Finding Lists begin on page ii.



Department of the Treasury
Internal Revenue Service

Announcement 2003-40, page 1132.

This announcement describes changes the IRS is testing under section 32 of the Code in determining qualifying child eligibility under the Earned Income Credit.

Announcement 2003-43, page 1139.

This announcement contains the annual report concerning the Pre-Filing Agreement Program of the Large and Mid-Size Business Division of the Service for Calendar Year 2002.

Announcement 2003-44, page 1144.

This document corrects a typographical error in Rev. Rul. 2003-50, 2003-21 I.R.B. 944. Rev. Rul. 2003-50 modified.

The IRS Mission

Provide America's taxpayers top quality service by helping them understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court

decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1986 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1986.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions and Other Related Items, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts. Also included in this part are Bank Secrecy Act Administrative Rulings. Bank Secrecy Act Administrative Rulings are issued by the Department of the Treasury's Office of the Assistant Secretary (Enforcement).

Part IV.—Items of General Interest.

This part includes notices of proposed rulemakings, disbarment and suspension lists, and announcements.

The first Bulletin for each month includes a cumulative index for the matters published during the preceding months. These monthly indexes are cumulated on a semiannual basis, and are published in the first Bulletin of the succeeding semiannual period, respectively.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1986

Section 472.—Last-in, First-out Inventories

26 CFR 1.472-1: Last-in, first-out inventories.

LIFO; price indexes; department stores. The April 2003 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, April 30, 2003.

Rev. Rul. 2003-68

The following Department Store Inventory Price Indexes for April 2003 were issued by the Bureau of Labor Statistics. The indexes are accepted by the Internal Revenue Service, under § 1.472-1(k) of the Income Tax Regulations and Rev. Proc. 86-46, 1986-2 C.B. 739, for appropriate application to inventories of department stores employing the retail inventory and last-in, first-out inventory methods for tax years ended on, or with reference to, April 30, 2003.

The Department Store Inventory Price Indexes are prepared on a national basis and include (a) 23 major groups of departments, (b) three special combinations of the major groups — soft goods, durable goods, and miscellaneous goods, and (c) a store total, which covers all departments, including some not listed separately, except for the following: candy, food, liquor, tobacco, and contract departments.

BUREAU OF LABOR STATISTICS, DEPARTMENT STORE
INVENTORY PRICE INDEXES BY DEPARTMENT GROUPS
(January 1941 = 100, unless otherwise noted)

Groups	Apr. 2002	Apr. 2003	Percent Change from Apr. 2002 to Apr. 2003 ¹
1. Piece Goods	488.7	457.9	-6.3
2. Domestics and Draperies	597.7	568.1	-5.0
3. Women's and Children's Shoes	652.6	646.4	-1.0
4. Men's Shoes	902.7	844.7	-6.4
5. Infants' Wear	622.2	597.8	-3.9
6. Women's Underwear	554.0	517.2	-6.6
7. Women's Hosiery	356.0	347.1	-2.5
8. Women's and Girls' Accessories	565.6	552.1	-2.4
9. Women's Outerwear and Girls' Wear	395.0	385.7	-2.4
10. Men's Clothing	600.2	569.0	-5.2
11. Men's Furnishings	604.4	589.8	-2.4
12. Boys' Clothing and Furnishings	504.2	465.5	-7.7
13. Jewelry	905.6	876.5	-3.2
14. Notions	794.8	794.1	-0.1
15. Toilet Articles and Drugs	974.7	982.5	0.8
16. Furniture and Bedding	627.7	627.7	0.0
17. Floor Coverings	618.7	584.4	-5.5
18. Housewares	756.6	730.3	-3.5
19. Major Appliances	222.6	215.3	-3.3
20. Radio and Television	50.8	46.4	-8.7
21. Recreation and Education ²	87.2	83.7	-4.0
22. Home Improvements ²	125.8	125.1	-0.6
23. Auto Accessories ²	110.8	111.5	0.6
Groups 1-15: Soft Goods	591.9	573.8	-3.1
Groups 16-20: Durable Goods	413.9	399.0	-3.6
Groups 21-23: Misc. Goods ²	97.1	94.8	-2.4
Store Total ³	526.3	510.0	-3.1

(Footnotes are on the following page.)

¹Absence of a minus sign before the percentage change in this column signifies a price increase.

²Indexes on a January 1986 = 100 base.

³The store total index covers all departments, including some not listed separately, except for the following: candy, food, liquor, tobacco and contract departments.

DRAFTING INFORMATION

The principal author of this revenue ruling is Michael Burkom of the Office of Associate Chief Counsel (Income Tax and Accounting). For further information regarding this revenue ruling, contact Mr. Burkom at (202) 622-7718 (not a toll-free call).

Section 755.—Rules for Allocation of Basis

26 CFR 1.755-1: Rules for allocation of basis.

T.D. 9059

DEPARTMENT OF THE TREASURY Internal Revenue Service 26 CFR Parts 1 and 602

Coordination of Sections 755 and 1060; Allocation of Basis Adjustments Among Partnership Assets and Application of the Residual Method to Certain Partnership Transactions

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations and removal of temporary regulations.

SUMMARY: This document finalizes regulations relating to the allocation of basis adjustments among partnership assets under section 755. The regulations are necessary to implement section 1060, which applies the residual method to certain partnership transactions.

DATES: These regulations are effective June 9, 2003.

FOR FURTHER INFORMATION CONTACT: Craig Gerson, (202) 622-3050 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

This document contains amendments to 26 CFR part 1 under section 755 of the In-

ternal Revenue Code (Code). On April 5, 2000, a notice of proposed rulemaking (REG-107872-99, 2000-1 C.B. 911 [65 FR 17829]) under section 755 was published in the **Federal Register**. Only one commentator submitted written comments in response to the notice of proposed rulemaking, and no public hearing was requested or held. After consideration of the comment, the proposed regulations are adopted as revised by this Treasury decision.

Explanation of Revisions and Summary of Contents

1. Summary

Section 743(b) provides for an optional adjustment to the basis of partnership property following certain transfers of partnership interests. The amount of the basis adjustment is the difference between the transferee's basis in the partnership interest and the transferee's share of the partnership's basis in the partnership's assets. Once the amount of the basis adjustment is determined, it is allocated among the partnership's individual assets pursuant to section 755.

On December 14, 1999, final regulations (T.D. 8847, 1999-2 C.B. 701 [64 FR 69903]) were published in the **Federal Register** under section 755. Under these regulations, basis adjustments under section 743(b) are allocated among a partnership's assets as follows. First, the adjustment is allocated between the two classes of property described in section 755(b). These classes of property consist of capital assets and section 1231(b) property (capital gain property), and any other property of the partnership (ordinary income property). The amount of a basis adjustment under section 743(b) that is allocated to the class of ordinary income property is equal to the total amount of income, gain, or loss that would be allocated to the transferee from the sale of all ordinary income property. The amount of the basis adjustment under section 743(b) that is allocated to capital gain property is the total amount of the basis adjustment under section 743(b) less the amount of the basis adjustment allo-

cated to ordinary income property. The basis adjustment is then allocated to individual assets within each class.

The final regulations issued on December 14, 1999, worked in conjunction with §1.755-2T. In the case of a basis adjustment under section 743(b) or section 732(d), the fair market values of all assets other than goodwill or going concern value were determined on the basis of all the facts and circumstances, and the fair market value of goodwill and going concern value was determined using the residual method. As described more fully in the notice of proposed rulemaking, §1.755-2T was published prior to the enactment of section 1060(d), which (as amended in 1993) requires the residual method to be applied for purposes of determining the values of section 197 intangibles for purposes of applying section 755. These final regulations implement section 1060(d) and replace §1.755-2T.

These final regulations differ from §1.755-2T by using the residual method to value all section 197 intangibles (not just goodwill and going concern value). In addition, these final regulations also apply to basis adjustments under section 734(b) and contain special rules for certain substituted basis transactions. Finally, for convenience, the provisions of the regulations have been relocated to the beginning of §1.755-1.

Under these final regulations, a partnership is required to assign values to its assets as follows. First, the partnership must determine the values of each of its assets other than section 197 intangibles under all the facts and circumstances, taking into account section 7701(g) (treating the fair market value of a property as not less than the amount of any nonrecourse indebtedness to which the property is subject). The partnership then must determine the gross value of all partnership assets (partnership gross value). Last, the partnership is required to use the residual method to assign values to the partnership's section 197 intangibles. For purposes of these regulations, the term *section 197 intangibles* includes all section 197 intangibles (as defined in section 197), as

well as any goodwill or going concern value that would not qualify as a section 197 intangible under section 197.

If the aggregate value of partnership property other than section 197 intangibles is equal to or greater than partnership gross value, then all section 197 intangibles are deemed to have a value of zero. In all other cases, the aggregate value of the partnership's section 197 intangibles (the residual section 197 intangibles value) is deemed to equal the excess of partnership gross value over the aggregate value of partnership property other than section 197 intangibles. The residual section 197 intangibles value must be allocated, first, among section 197 intangibles other than goodwill and going concern value. Any remaining value is assigned to goodwill and going concern value.

The proposed regulations used the residual method to assign values to all partnership assets, rather than limiting the scope of the residual method to section 197 intangibles. Treasury and the IRS have concluded that these rules were unduly complex, especially when they applied to partnerships whose partnership agreements contained special allocations of partnership income or loss. Accordingly, the final regulations utilize the residual method only to value section 197 intangibles.

2. Transactions Subject to the Regulations

Because the proposed regulations used the residual method to value all partnership assets (and not just section 197 intangibles), it was desirable for all partnerships to value their assets using the same method. Accordingly, under the authority of sections 1060(d) and 755, the proposed regulations applied to all partnerships, whether or not their assets constituted a trade or business. In contrast, the final regulations apply the residual method only for the purpose of valuing section 197 intangibles, which are usually held by partnerships whose assets constitute a trade or business. Thus, the final regulations apply the residual method only to partnerships whose assets constitute a trade or business (as described in §1.1060-1(b)(2)).

The proposed regulations specifically applied to basis adjustments under section 732(d). Some references to section 732(d) have been removed in the final regulations to enhance readability. Neverthe-

less, the final regulations continue to apply to basis adjustments under section 732(d).

3. Methods for Determining Partnership Gross Value

If a partnership interest is transferred in a taxable transaction, the transferee's basis in its partnership interest provides a frame of reference for determining partnership gross value. In these transactions, both the proposed and the final regulations generally provide that partnership gross value is the amount that, if assigned to all partnership property, would result in a liquidating distribution to the transferee partner equal to that partner's basis (reduced by the amount, if any, of such basis that is attributable to partnership liabilities) in the transferred partnership interest immediately following the relevant transfer.

In certain circumstances involving basis adjustments under section 743(b), such as where income or loss with respect to particular section 197 intangibles is allocated differently among partners, partnership gross value may vary depending on the fair market values of particular section 197 intangibles held by the partnership. In these situations, the final regulations require the partnership to use a reasonable method, consistent with the purposes of the final regulations, to determine partnership gross value.

In the preamble to the proposed regulations, the IRS and the Treasury Department requested comments regarding how the residual method applies in the context of a basis adjustment that results from an exchange of a partnership interest in which the transferee's basis in the interest is determined in whole or in part by reference to the transferor's basis in the interest (a transferred basis exchange). Determining partnership gross value in such an exchange is problematic, because the transferee's basis in the partnership interest does not necessarily have any connection to the fair market values of partnership assets. No comments were received regarding the specific method to be adopted by the final regulations.

The IRS and the Treasury Department also requested comments regarding how the residual method applies in the context of basis adjustments under section 734(b). One commentator suggested that the final regulations should require one method for valuing partnership assets in the case of a "pro

rata" distribution, and another method for valuing partnership assets in the case of a "non-pro rata" distribution. The IRS and the Treasury Department believe that this approach would be unnecessarily complex.

The final regulations adopt a single method for determining partnership gross value that applies to all section 734(b) basis adjustments and to section 743(b) basis adjustments resulting from transferred basis exchanges. In these circumstances, partnership gross value is the value of the entire partnership as a going concern, increased by the amount of partnership liabilities. In the case of a basis adjustment under section 734(b), the value of the entire partnership as a going concern is determined immediately after the distribution causing the adjustment.

A commentator has suggested that the same method for determining partnership gross value should apply to exchanged basis transactions, such as the distribution of a partnership interest by a partnership. The final regulations adopt this comment by replacing all references to transferred basis exchanges with references to substituted basis transactions. Conforming adjustments are also made to the special rules contained in §1.755-1(b)(5) for allocating basis adjustments under section 743(b) among a partnership's assets in these exchanges.

4. Transferors of Partnership Interests

In the preamble to the proposed regulations, comments were requested as to whether the residual method should be used to determine the fair market values of partnership assets for purposes of applying section 1(h)(6)(B) (collectibles gain or loss), section 1(h)(7) (section 1250 capital gain), and section 751(a) (ordinary income) to the sale or other disposition of a partnership interest. No comments were received on this issue. Treasury and the IRS have determined that the potential benefits of a rule allowing transferors to use the residual method do not justify the increased complexity that the rule would have created.

5. Other Changes

The final regulations add two clarifying rules for allocating basis adjustments under section 743(b) among a partnership's assets in the case of a transaction that is not a substituted basis transaction. The first rule provides that assets with respect to which

the transferee partner has no interest in income, gain, losses, or deductions are not taken into account in allocating basis adjustments to capital assets. The second rule provides that in no event may the amount of any decrease in basis allocated to an item of capital gain property exceed the partnership's adjusted basis in that item. If the amount of a decrease in basis otherwise allocable to a particular capital asset exceeds the partnership's adjusted basis in that asset, the transferee's negative basis adjustment in that asset is limited to the partnership's adjusted basis in that asset, and the excess must be applied to reduce the remaining basis, if any, of other capital gain assets *pro rata* in proportion to the partnership's adjusted bases in such assets.

Effective Date

These regulations apply to transfers of partnership interests and distributions of property from partnerships that occur on or after June 9, 2003.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and because the regulations do not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Internal Revenue Code, the notice of proposed rulemaking preceding these regulations was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small businesses.

Drafting Information

The principal author of these regulations is Craig Gerson of the Office of the Associate Chief Counsel (Passthroughs and Special Industries). However, personnel from other offices of the IRS and the Treasury Department participated in their development.

* * * * *

Adoption of Amendments to the Regulations

Accordingly, 26 CFR parts 1 and 602 are amended as follows:

PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 is amended by adding an entry to read in part as follows:

Authority: 26 U.S.C. 7805. * * *

Section 1.755-2 also issued under 26 U.S.C. 755 and 26 U.S.C. 1060. * * *

Par. 2. Section 1.755-1 is amended as follows:

1. Paragraph (a) is revised.

2-3. A paragraph heading is added for paragraph (b)(1)(i).

4. The first two sentences of paragraph (b)(1)(i) are revised.

5. Paragraph (b)(3)(iii) is redesignated as paragraph (b)(3)(iv).

6. New paragraph (b)(3)(iii) is added.

7. In paragraph (b)(4)(ii), the *Example* is revised.

8. The paragraph heading for paragraph (b)(5) is revised.

9. Paragraph (b)(5)(i) is revised.

10. In paragraph (b)(5)(iv) *Example 1*, the last sentence is amended by removing the language "transferred basis exchange" and adding "substituted basis transaction" in its place.

11. In paragraph (b)(5)(iv) *Example 2*, paragraph (iii), the third sentence is amended by adding the language "this" before the language "paragraph (b)(5)".

12. In paragraph (c)(5) *Example (i)* introductory text is revised.

13. Paragraph (d) is revised.

14. Paragraph (e) is added.

The revisions and additions read as follows:

§1.755-1 Rules for allocation of basis.

(a) *In general*—(1) *Scope*. This section provides rules for allocating basis adjustments under sections 743(b) and 734(b) among partnership property. If there is a basis adjustment to which this section applies, the basis adjustment is allocated among the partnership's assets as follows. First, the partnership must determine the value of each of its assets under paragraphs (a)(2) through (5) of this section. Second, the basis adjustment is allocated between the two classes of property described in section 755(b). These classes of property consist of capital assets and section 1231(b) property (capital gain property), and any other property of the partnership (ordinary income property). For purposes of this section, properties and potential gain treated

as unrealized receivables under section 751(c) and the regulations thereunder shall be treated as separate assets that are ordinary income property. Third, the portion of the basis adjustment allocated to each class is allocated among the items within the class. Basis adjustments under section 743(b) are allocated among partnership assets under paragraph (b) of this section. Basis adjustments under section 734(b) are allocated among partnership assets under paragraph (c) of this section.

(2) *Coordination of sections 755 and 1060*. If there is a basis adjustment to which this section applies, and the assets of the partnership constitute a trade or business (as described in §1.1060-1(b)(2)), then the partnership is required to use the residual method to assign values to the partnership's section 197 intangibles. To do so, the partnership must, first, determine the value of partnership assets other than section 197 intangibles under paragraph (a)(3) of this section. The partnership then must determine partnership gross value under paragraph (a)(4) of this section. Last, the partnership must assign values to the partnership's section 197 intangibles under paragraph (a)(5) of this section. For purposes of this section, the term *section 197 intangibles* includes all section 197 intangibles (as defined in section 197), as well as any goodwill or going concern value that would not qualify as a section 197 intangible under section 197.

(3) *Values of properties other than section 197 intangibles*. For purposes of this section, the fair market value of each item of partnership property other than section 197 intangibles shall be determined on the basis of all the facts and circumstances, taking into account section 7701(g).

(4) *Partnership gross value*—(i) *Basis adjustments under section 743(b)*—(A) *In general*. Except as provided in paragraph (a)(4)(ii) of this section, in the case of a basis adjustment under section 743(b), partnership gross value generally is equal to the amount that, if assigned to all partnership property, would result in a liquidating distribution to the partner equal to the transferee's basis in the transferred partnership interest immediately following the relevant transfer (reduced by the amount, if any, of such basis that is attributable to partnership liabilities).

(B) *Special situations*. In certain circumstances, such as where income or loss

with respect to particular section 197 intangibles are allocated differently among partners, partnership gross value may vary depending on the values of particular section 197 intangibles held by the partnership. In these special situations, the partnership must assign value, first, among section 197 intangibles (other than goodwill and going concern value) in a reasonable manner that is consistent with the ordering rule in paragraph (a)(5) of this section and would cause the appropriate liquidating distribution under paragraph (a)(4)(i)(A) of this section. If the actual fair market values, determined on the basis of all the facts and circumstances, of all section 197 intangibles (other than goodwill and going concern value) is not sufficient to cause the appropriate liquidating distribution, then the fair market value of goodwill and going concern value shall be presumed to equal an amount that if assigned to goodwill and going concern value would cause the appropriate liquidating distribution.

(C) *Income in respect of a decedent.* Solely for the purpose of determining partnership gross value under this paragraph (a)(4)(i), where a partnership interest is transferred as a result of the death of a partner, the transferee's basis in its partnership interest is determined without regard to section 1014(c), and is deemed to be adjusted for that portion of the interest, if any, that is attributable to items representing income in respect of a decedent under section 691.

(ii) *Basis adjustments under section 743(b) resulting from substituted basis transactions.* This paragraph (a)(4)(ii) applies to basis adjustments under section 743(b) that result from exchanges in which the transferee's basis in the partnership interest is determined in whole or in part by reference to the transferor's basis in the interest or to the basis of other property held at any time by the transferee (substituted basis transactions). In the case of a substituted basis transaction, partnership gross value equals the value of the entire partnership as a going concern, increased by the amount of partnership liabilities at the time of the exchange giving rise to the basis adjustment.

(iii) *Basis adjustments under section 734(b).* In the case of a basis adjustment under section 734(b), partnership gross value equals the value of the entire partnership

as a going concern immediately following the distribution causing the adjustment, increased by the amount of partnership liabilities immediately following the distribution.

(5) *Determining the values of section 197 intangibles—(i) Two classes.* If the aggregate value of partnership property other than section 197 intangibles (as determined in paragraph (a)(3) of this section) is equal to or greater than partnership gross value (as determined in paragraph (a)(4) of this section), then all section 197 intangibles are deemed to have a value of zero for purposes of this section. In all other cases, the aggregate value of the partnership's section 197 intangibles (the residual section 197 intangibles value) is deemed to equal the excess of partnership gross value over the aggregate value of partnership property other than section 197 intangibles. The residual section 197 intangibles value must be allocated between two asset classes in the following order —

(A) Among section 197 intangibles other than goodwill and going concern value; and

(B) To goodwill and going concern value.

(ii) *Values assigned to section 197 intangibles other than goodwill and going concern value.* The fair market value assigned to a section 197 intangible (other than goodwill and going concern value) shall not exceed the actual fair market value (determined on the basis of all the facts and circumstances) of that asset on the date of the relevant transfer. If the residual section 197 intangibles value is less than the sum of the actual fair market values (determined on the basis of all the facts and circumstances) of all section 197 intangibles (other than goodwill and going concern value) held by the partnership, then the residual section 197 intangibles value must be allocated among the individual section 197 intangibles (other than goodwill and going concern value) as follows. The residual section 197 intangibles value is assigned first to any section 197 intangibles (other than goodwill and going concern value) having potential gain that would be treated as unrealized receivables under the flush language of section 751(c) (flush language receivables) to the extent of the basis of those section 197 intangibles and the amount of income arising from the flush language receivables that the partnership would recognize if the section 197 intan-

gibles were sold for their actual fair market values (determined based on all the facts and circumstances) (collectively, the flush language receivables value). If the value assigned to section 197 intangibles (other than goodwill and going concern value) is less than the flush language receivables value, then the assigned value is allocated among the properties giving rise to the flush language receivables in proportion to the flush language receivables value in those properties. Any remaining residual section 197 intangibles value is allocated among the remaining portions of the section 197 intangibles (other than goodwill and going concern value) in proportion to the actual fair market values of such portions (determined based on all the facts and circumstances).

(iii) *Value assigned to goodwill and going concern value.* The fair market value of goodwill and going concern value is the amount, if any, by which the residual section 197 intangibles value exceeds the aggregate value of the partnership's section 197 intangibles (other than goodwill and going concern value).

(6) *Examples.* The provisions of paragraphs (a)(2) through (5) are illustrated by the following examples, which assume that the partnerships have an election in effect under section 754 at the time of the transfer and that the assets of each partnership constitute a trade or business (as described in §1.1060-1(b)(2)). Except as provided, no partnership asset (other than inventory) is property described in section 751(a), and partnership liabilities are secured by all partnership assets. The examples are as follows:

Example 1. (i) A is the sole general partner in PRS, a limited partnership having three equal partners. PRS has goodwill and going concern value, two section 197 intangibles other than goodwill and going concern value (Intangible 1 and Intangible 2), and two other assets with fair market values (determined using all the facts and circumstances) as follows: inventory worth \$1,000,000 and a building (a capital asset) worth \$2,000,000. The fair market value of each of Intangible 1 and Intangible 2 is \$50,000. PRS has one liability of \$1,000,000, for which A bears the entire risk of loss under section 752 and the regulations thereunder. D purchases A's partnership interest for \$650,000, resulting in a basis adjustment under section 743(b). After the purchase, D bears the entire risk of loss for PRS's liability under section 752 and the regulations thereunder. Therefore, D's basis in its interest in PRS is \$1,650,000.

(ii) D's basis in the transferred partnership interest (reduced by the amount of such basis that is attributable to partnership liabilities) is \$650,000 (\$1,650,000 - \$1,000,000). Under paragraph (a)(4)(i) of this section, partnership gross value is \$2,950,000

(the amount that, if assigned to all partnership property, would result in a liquidating distribution to D equal to \$650,000).

(iii) Under paragraph (a)(3) of this section, the inventory has a fair market value of \$1,000,000, and the building has a fair market value of \$2,000,000. Thus, the aggregate value of partnership property other than section 197 intangibles, \$3,000,000, is equal to or greater than partnership gross value, \$2,950,000. Accordingly, under paragraphs (a)(3) and (5) of this section, the value assigned to each of the partnership's assets is as follows: inventory, \$1,000,000; building, \$2,000,000; Intangibles 1 and 2, \$0; and goodwill and going concern value, \$0. D's section 743(b) adjustment must be allocated under paragraph (b) of this section using these assigned fair market values.

Example 2. (i) Assume the same facts as in *Example 1*, except that the fair market values of Intangible 1 and Intangible 2 are each \$300,000, and that D purchases A's interest in PRS for \$1,000,000. After the purchase, D's basis in its interest in PRS is \$2,000,000.

(ii) D's basis in the transferred partnership interest (reduced by the amount of such basis that is attributable to partnership liabilities) is \$1,000,000 (\$2,000,000 - \$1,000,000). Under paragraph (a)(4)(i) of this section, partnership gross value is \$4,000,000 (the amount that, if assigned to all partnership property, would result in a liquidating distribution to D equal to \$1,000,000).

(iii) Under paragraph (a)(5) of this section, the residual section 197 intangibles value is \$1,000,000 (the excess of partnership gross value, \$4,000,000, over the aggregate value of assets other than section 197 intangibles, \$3,000,000 (the sum of the value of the inventory, \$1,000,000, and the value of the building, \$2,000,000)). The partnership must determine the values of section 197 assets by allocating the residual section 197 intangibles value among the partnership's assets. The residual section 197 intangibles value is assigned first to section 197 intangibles other than goodwill and going concern value, and then to goodwill and going concern value. Thus, \$300,000 is assigned to each of Intangible 1 and Intangible 2, and \$400,000 is assigned to goodwill and going concern value (the amount by which the residual section 197 intangibles value, \$1,000,000, exceeds the fair market value of section 197 intangibles other than goodwill and going concern value, \$600,000). D's section 743(b) adjustment must be allocated under paragraph (b) of this section using these assigned fair market values.

Example 3. (i) Assume the same facts as in *Example 1*, except that the fair market values of Intangible 1 and Intangible 2 are each \$300,000, and that D purchases A's interest in PRS for \$750,000. After the purchase, D's basis in its interest in PRS is \$1,750,000. Also assume that Intangible 1 was originally purchased for \$300,000, and that its adjusted basis has been decreased to \$50,000 as a result of amortization. Assume that, if PRS were to sell Intangible 1 for \$300,000, it would recognize \$250,000 of gain that would be treated as an unrealized receivable under the flush language in section 751(c).

(ii) D's basis in the transferred partnership interest (reduced by the amount of such basis that is attributable to partnership liabilities) is \$750,000 (\$1,750,000 - \$1,000,000). Under paragraph (a)(4)(i) of this section, partnership gross value is \$3,250,000

(the amount that, if assigned to all partnership property, would result in a liquidating distribution to D equal to \$750,000).

(iii) Under paragraph (a)(5) of this section, the residual section 197 intangibles value is \$250,000 (the amount by which partnership gross value, \$3,250,000, exceeds the aggregate value of partnership property other than section 197 intangibles, \$3,000,000). Intangible 1 has potential gain that would be treated as unrealized receivables under the flush language of section 751(c). The flush language receivables value in Intangible 1 is \$300,000 (the sum of PRS's basis in Intangible 1, \$50,000, and the amount of ordinary income, \$250,000, that the partnership would recognize if Intangible 1 were sold for its actual fair market value). Because the residual section 197 intangibles value, \$250,000, is less than the flush language receivables value of Intangible 1, Intangible 1 is assigned a value of \$250,000, and Intangible 2 and goodwill and going concern value are assigned a value of zero. D's section 743(b) adjustment must be allocated under paragraph (b) of this section using these assigned fair market values.

Example 4. Assume the same facts as in *Example 1*, except that the fair market values of Intangible 1 and Intangible 2 are each \$300,000, and that A does not sell its interest in PRS. Instead, A contributes its interest in PRS to E, a newly formed corporation wholly-owned by A, in a transaction described in section 351. Assume that the contribution results in a basis adjustment under section 743(b) (other than zero). PRS determines that its value as a going concern immediately following the contribution is \$3,000,000. Under paragraph (a)(4)(ii) of this section, partnership gross value is \$4,000,000 (the value of PRS as a going concern, \$3,000,000, increased by the partnership's liability, \$1,000,000, immediately after the contribution). Under paragraph (a)(5) of this section, the residual section 197 intangibles value is \$1,000,000 (the amount by which partnership gross value, \$4,000,000, exceeds the aggregate value of partnership property other than section 197 intangibles, \$3,000,000). Of the residual section 197 intangibles value, \$300,000 is assigned to each of Intangible 1 and Intangible 2, and \$400,000 is assigned to goodwill and going concern value (the amount by which the residual section 197 intangibles value, \$1,000,000, exceeds the fair market value of section 197 intangibles other than goodwill and going concern value, \$600,000). E's section 743(b) adjustment must be allocated under paragraph (b)(5) of this section using these assigned fair market values.

Example 5. G is the sole general partner in PRS, a limited partnership having three equal partners (G, H, and I). PRS has goodwill and going concern value, two section 197 intangibles other than goodwill and going concern value (Intangible 1 and Intangible 2), and two capital assets with fair market values (determined using all the facts and circumstances) as follows: vacant land worth \$1,000,000, and a building worth \$2,000,000. The fair market value of each of Intangible 1 and Intangible 2 is \$300,000. PRS has one liability of \$1,000,000, for which G bears the entire risk of loss under section 752 and the regulations thereunder. PRS distributes the land to H in liquidation of H's interest in PRS. Immediately prior to the distribution, PRS's basis in the land is \$800,000, and H's basis in its interest in PRS is \$750,000. The distribution causes the partnership to increase the basis of its remaining property by \$50,000 under sec-

tion 734(b)(1)(B). PRS determines that its value as a going concern immediately following the distribution is \$2,000,000. Under paragraph (a)(4)(iii) of this section, partnership gross value is \$3,000,000 (the value of PRS as a going concern, \$2,000,000, increased by the partnership's liability, \$1,000,000, immediately after the distribution). Under paragraph (a)(5) of this section, the residual section 197 intangibles value of PRS's section 197 intangibles is \$1,000,000 (the amount by which partnership gross value, \$3,000,000, exceeds the aggregate value of partnership property other than section 197 intangibles, \$2,000,000). Of the residual section 197 intangibles value, \$300,000 is assigned to each of Intangible 1 and Intangible 2, and \$400,000 is assigned to goodwill and going concern value (the amount by which the residual section 197 intangibles value, \$1,000,000, exceeds the fair market value of section 197 intangibles other than goodwill and going concern value, \$600,000). PRS's section 734(b) adjustment must be allocated under paragraph (c) of this section using these assigned fair market values.

(b) *Adjustments under section 743(b)*—
(1) *Generally*—(i) *Application.* For basis adjustments under section 743(b) resulting from substituted basis transactions, paragraph (b)(5) of this section shall apply. For basis adjustments under section 743(b) resulting from all other transfers, paragraphs (b)(2) through (4) of this section shall apply. * * *

* * * * *
(3) * * *

(iii) *Special rules*—(A) *Assets in which partner has no interest.* An asset with respect to which the transferee partner has no interest in income, gain, losses, or deductions shall not be taken into account in applying paragraph (b)(3)(ii)(B) of this section.

(B) *Limitation in decrease of basis.* In no event may the amount of any decrease in basis allocated to an item of capital gain property under paragraph (b)(3)(ii)(B) of this section exceed the partnership's adjusted basis in that item (or in the case of property subject to the remedial allocation method, the transferee's share of any remedial loss under §1.704-3(d) from the hypothetical transaction). In the event that a decrease in basis allocated under paragraph (b)(3)(ii)(B) of this section to an item of capital gain property would otherwise exceed the partnership's adjusted basis in that item, the excess must be applied to reduce the remaining basis, if any, of other capital gain assets *pro rata* in proportion to the bases of such assets (as adjusted under this paragraph (b)(3)).

* * * * *
(4) * * *
(ii) * * *

Example. (i) A and B are equal partners in personal service partnership PRS.

In 2004, as a result of B's death, B's partnership interest is transferred to T when PRS's balance sheet (reflecting a cash receipts and disbursements method

of accounting) is as follows (based on all the facts and circumstances):

Assets		
	Adjusted Basis	Fair Market Value
Section 197 Intangible	\$2,000	\$ 5,000
Unrealized Receivables	<u>0</u>	<u>15,000</u>
Total	\$2,000	\$20,000
Liabilities and Capital		
	Adjusted Per Books	Fair Market Value
Capital:		
A	1,000	10,000
B	<u>1,000</u>	<u>10,000</u>
Total	\$2,000	\$20,000

(ii) None of the assets owned by PRS is section 704(c) property, and the section 197 intangible is not amortizable. The fair market value of T's partnership interest on the applicable date of valuation set forth in section 1014 is \$10,000. Of this amount, \$2,500 is attributable to T's 50% share of the partnership's section 197 intangible, and \$7,500 is attributable to T's 50% share of the partnership's unrealized receivables. The partnership's unrealized receivables represent income in respect of a decedent. Accordingly, under section 1014(c), T's basis in its partnership interest is not adjusted for that portion of the interest which is attributable to the unrealized receivables. Therefore, T's basis in its partnership interest is \$2,500.

(iii) Under paragraph (a)(4)(i)(C) of this section, solely for purposes of determining partnership gross value, T's basis in its partnership interest is deemed to be \$10,000. Under paragraph (a)(4)(i) of this section, partnership gross value is \$20,000 (the amount that, if assigned to all partnership property, would result in a liquidating distribution to T equal to \$10,000).

(iv) Under paragraph (a)(5) of this section, the residual section 197 intangibles value is \$5,000 (the excess of partnership gross value, \$20,000, over the aggregate value of assets other than section 197 intangibles, \$15,000). The residual section 197 intangibles value is assigned first to section 197 intangibles other than goodwill and going concern value, and then to goodwill and going concern value. Thus, \$5,000 is assigned to the section 197 intangible, and \$0 is assigned to goodwill and going concern value. T's section 743(b) adjustment must be allocated using these assigned fair market values.

(v) At the time of the transfer, B's share of the partnership's basis in partnership assets is \$1,000. Accordingly, T receives a \$1,500 basis adjustment under section 743(b). Under this paragraph (b)(4), the entire basis adjustment is allocated to the partnership's section 197 intangible.

(5) *Substituted basis transactions*—(i) *In general.* This paragraph (b)(5) applies to ba-

sis adjustments under section 743(b) that result from exchanges in which the transferee's basis in the partnership interest is determined in whole or in part by reference to the transferor's basis in that interest. For exchanges on or after June 9, 2003, this paragraph (b)(5) also applies to basis adjustments under section 743(b) that result from exchanges in which the transferee's basis in the partnership interest is determined by reference to other property held at any time by the transferee. For example, this paragraph (b)(5) applies if a partnership interest is contributed to a corporation in a transaction to which section 351 applies, if a partnership interest is contributed to a partnership in a transaction to which section 721(a) applies, or if a partnership interest is distributed by a partnership in a transaction to which section 731(a) applies.

* * * * *

(c) * * *

(5) * * *

Example. (i) A, B, and C form equal partnership PRS. A contributes \$50,000 and Asset 1, nondepreciable capital gain property with a fair market value of \$50,000 and an adjusted tax basis of \$25,000. B and C each contributes \$100,000. PRS uses the cash to purchase Assets 2, 3, 4, 5, and 6. Assets 2 and 3 are nondepreciable capital assets, and Assets 4, 5, and 6 are inventory that has not appreciated substantially in value within the meaning of section 751(b)(3). Assets 4, 5, and 6 are the only assets held by the partnership that are subject to section 751. The partnership has an election in effect under section 754. Af-

ter seven years, the adjusted basis and fair market value of PRS's assets are as follows:

* * * * *

(d) *Required statements.* See §1.743-1(k)(2) for provisions requiring the transferee of a partnership interest to provide information to the partnership relating to the transfer of an interest in the partnership. See §1.743-1(k)(1) for a provision requiring the partnership to attach a statement to the partnership return showing the computation of a basis adjustment under section 743(b) and the partnership properties to which the adjustment is allocated under section 755. See §1.732-1(d)(3) for a provision requiring a transferee partner to attach a statement to its return showing the computation of a basis adjustment under section 732(d) and the partnership properties to which the adjustment is allocated under section 755. See §1.732-1(d)(5) for a provision requiring the partnership to provide information to a transferee partner reporting a basis adjustment under section 732(d).

(e) *Effective Date*—(1) *Generally.* Except as provided in paragraphs (b)(5) and (e)(2) of this section, this section applies to transfers of partnership interests and distributions of property from a partnership that occur on or after December 15, 1999.

(2) *Special rules.* Paragraphs (a) and (b)(3)(iii) of this section apply to transfers of partnership interests and distributions of property from a partnership that occur on or after June 9, 2003.

§1.755-2T [Removed]

Par. 3. Section 1.755-2T is removed.

Par. 4. In §1.1060-1, paragraph (e)(2) is revised to read as follows:

§1.1060-1 Special allocation rules for certain asset acquisitions.

* * * * *

(e) * * *

(2) *Transfers of interests in partnerships.* For reporting requirements relating to the transfer of a partnership interest, see §1.755-1(d).

PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Par. 5. The authority citation for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

602.101 [Amended]

Par. 6. In §602.101, paragraph (b), the entry for “1.755-2T” is removed.

David A. Mader,
Assistant Deputy Commissioner of
Internal Revenue.

Approved May 22, 2003.

Pamela F. Olson,
Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on June 6, 2003, 8:45 a.m., and published in the issue of the Federal Register for June 9, 2003, 68 F.R. 34293)

Section 6041A.—Returns Regarding Payments of Remuneration for Services and Direct Sales

(Also: 6050M.)

26 CFR 1.6041A-1: Return of information as to payments of \$600 or more.

(Also: 1.6050M-1.)

Information reporting requirements.

This ruling provides guidance to federal agencies about the information reporting requirements under sections 6041A and 6050M of the Code for the payment of services.

Rev. Rul. 2003-66

PURPOSE

This revenue ruling provides guidance to federal agencies about the information

reporting requirements under sections 6041A and 6050M of the Internal Revenue Code. This revenue ruling clarifies that sections 6041A and 6050M impose separate information reporting requirements and have different underlying purposes and that, in some cases, the required information may overlap.

ISSUE

When is a federal executive agency required to report under sections 6041A and 6050M?

FACTS

Agency X is a federal executive agency of the United States as defined by section 6050M(b), which is (1) any Executive agency (as defined in section 105 of title 5, United States Code) other than the General Accounting Office, (2) any military department (as defined in section 102 of such title), and (3) the United States Postal Service and the Postal Rate Commission of the United States. All payments are made during the same calendar year.

Situation 1. Agency X pays Corporation A for cleaning services. The contract between Agency X and Corporation A provides that the total payment for the services is \$30,000.

Situation 2. Agency X pays Corporation B for the purchase of computer equipment. The contract requires a total payment of \$25,000 for the computer equipment.

Situation 3. Agency X pays Corporation C for repairs to one of the agency's automobiles. The repairs include the replacement of parts. The agency pays \$1000 for the repairs of which \$700 is for services.

None of the situations described above fall within the exception under section 6050M(e).

LAW

Section 6041A(a) provides that if (1) any service-recipient engaged in a trade or business pays in the course of such trade or business during any calendar year remuneration to any person for services performed by such person, and (2) the aggregate of such remuneration paid to such person during such calendar year is \$600 or more, then the service-recipient must file a return, according to the forms or regulations prescribed by the Secretary, set-

ting forth the aggregate amount of such payments and the name and address of the recipient of such payments. For purposes of the preceding sentence, the term “service-recipient” means the person for whom the service is performed. This information must be filed on Form 1099-MISC, *Miscellaneous Income*.

Section 6041A(d)(1) provides that the term “person” includes any governmental unit (and any agency or instrumentality thereof). Section 6041A(d)(2) provides that in the case of any payment by a governmental entity or any agency or instrumentality thereof (A) section 6041A(a) shall be applied without regard to the trade or business requirement contained therein, and (B) any return under section 6041A shall be made by the officer or employee having control of the payment or appropriately designated for the purpose of making such return.

Section 6041A(d)(3)(A) provides that section 6041A(a) shall apply to remuneration paid to a corporation by any federal executive agency (as defined in section 6050M(b)).

Section 6050M(a) provides that the head of every federal executive agency which enters into any contract shall make a return setting forth (1) the name, address, and TIN of each person with which such agency entered into a contract during the calendar year, and (2) such other information as the Secretary may require. This information must be filed on Form 8596, *Information Return for Federal Contracts*. See Treas. Reg. § 1.6050M-1(d).

Section 1.6050M-1(b)(2) of the Income Tax Regulations defines a “contract” as an obligation of a federal executive agency to make payment of money (or other property) to a person in return for the sale of property, the rendering of services, or other consideration.

Section 1.6050M-1(c)(1)(i) limits the information reporting requirement of section 6050M by providing that any contract or contract action for which the amount obligated is \$25,000 or less does not have to be reported.

Sections 6041A and 6050M are separate reporting requirements and differ in their primary purpose. The purpose of section 6041A is to identify unreported income. See S. Rep. No. 494, 97th Cong., 2d Sess. 247 (1982), July 12, 1982 (Senate Report). The purpose of section 6050M is to

provide the IRS with information concerning sources from which it can collect delinquent taxes owed by federal contractors. See H.R. Rep. No. 426, 99th Congress, 1st Sess. 855 (1985), 1986-3 (Vol. 2) C.B. 855.

ANALYSIS

Situation 1. The payment for the contracted cleaning services is subject to information reporting under section 6041A because the agency's payment for services exceeds the \$600 threshold. Agency X must file Form 1099-MISC. In addition, upon entering into the contract, Agency X is subject to information reporting under section 6050M because the contracted amount exceeds the \$25,000 threshold. Agency X must file Form 8596.

Situation 2. The payment for the purchase of computer equipment is not subject to information reporting under section 6041A because the payment is not for services. The contract is not subject to information reporting under section 6050M because the agency did not enter into a contract obligating an amount exceeding \$25,000. Agency X does not have to file either Form 1099-MISC or Form 8596.

Situation 3. The payment for the automobile repairs is subject to information reporting under section 6041A because the portion attributable to services exceeds the \$600 threshold. Agency X must file Form 1099-MISC. Agency X is not subject to section 6050M because the agency did not enter into a contract obligating an amount exceeding \$25,000. Agency X does not have to file Form 8596.

HOLDING

Sections 6041A and 6050M are separate information reporting requirements. Thus, with respect to a contract and the payments under that contract, a federal agency may be required, depending on the circumstances, to make an information return only under section 6041A, only under section 6050M, under both provisions, or under neither provision.

DRAFTING INFORMATION

The principal author of this revenue procedure is Tiffany P. Smith of the Office of the Associate Chief Counsel (Procedure and Administration), Administrative Provi-

sions and Judicial Practice Division. For further information regarding this revenue procedure, contact Tiffany P. Smith at (202) 622-4910 (not a toll-free call).

Section 6050M.—Returns Relating to Persons Receiving Contracts From Federal Executive Agencies

Guidance is provided to federal agencies about the information reporting requirements under sections 6041A and 6050M of the Internal Revenue Code. This ruling clarifies that sections 6041A and 6050M impose separate information reporting requirements and have different underlying purposes and that, in some cases, the required information may overlap. See Rev. Rul. 2003-66, page 1115.

Section 6103.—Confidentiality and Disclosure of Returns and Return Information

26 CFR 301.6103(j)(5)-1T: Disclosures of return information reflected on returns to officers and employees of the Department of Agriculture for conducting the census of agriculture (temporary).

T.D. 9060

DEPARTMENT OF THE TREASURY Internal Revenue Service 26 CFR Part 301

Disclosure of Return Information to the Department of Agriculture

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final and temporary regulations.

SUMMARY: This document contains regulations that incorporate and clarify the phrase "return information reflected on returns" in conformance with the terms of section 6103(j)(5) of the Internal Revenue Code (Code). These temporary regulations also remove certain items of return information that the IRS currently discloses, but the Department of Agricul-

ture no longer needs, for conducting the census of agriculture. The text of the temporary regulations serves as the text of the proposed regulations (REG-103809-03) set forth on page 1132 of this issue of the Bulletin.

DATES: *Effective Date:* These regulations are effective on June 6, 2003.

FOR FURTHER INFORMATION CONTACT: Christine Irwin at (202) 622-4570 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

These temporary regulations incorporate the phrase "return information reflected on returns" into §301.6103(j)(5)-1 in conformance with the statutory language that describes the type of return information that the IRS may disclose to the Department of Agriculture under section 6103(j)(5) of the Code. These temporary regulations are consistent with a recent clarification of the same phrase (*i.e.*, return information reflected on returns) in §301.6103(j)(1)-1, involving the disclosure of return information to the Bureau of the Census. See 68 FR 2691 (T.D. 9037, 2003-9 I.R.B. 535).

Also, currently §301.6103(j)(5)-1 provides an itemized description of the return information authorized for disclosure in conjunction with the census of agriculture. These temporary regulations remove certain items of return information currently listed in §301.6103(j)(5)-1 that the Department of Agriculture no longer needs in conjunction with the census of agriculture.

Explanation of Provisions

These temporary regulations adopt the phrase "return information reflected on returns" in lieu of the phrase "return information" that currently appears in §301.6103(j)(5)-1. (The phrase "return information reflected on returns" encompasses the phrase "return information reflected thereon" in section 6103(j)(5) of the Code.) These temporary regulations clarify the phrase "return information reflected on returns" by explaining that the phrase includes, but is not limited to, information on returns, information derived from processing such returns, and information derived from other sources for the purposes of establishing and maintaining taxpayer infor-

mation relating to returns. The phrase includes information derived from returns, monthly corrections of, and additions to, taxpayer information contained in IRS databases (e.g., taxpayer address and name changes) that are obtained from other sources, and computer codes the IRS derives from returns and/or tax forms and integrates within taxpayer data bases.

On March 4, 2003, and March 17, 2003, the Department of Agriculture's National Agriculture Statistics Service (NASS) notified the IRS that certain items of return information that are currently listed in §301.6103(j)(5)–1 are no longer needed in conjunction with the census of agriculture. Specifically, the Department of Agriculture no longer needs the following items currently extracted from IRS forms: (1) From Form 1040, Schedule F (*Profit or Loss From Farming*): sales of livestock and produce raised; (2) From Form 1120 series: Parent corporation Employer Identification Number, and related Name and Principal Business Activity (PBA) code for entities with agricultural activity; and (3) From Form 851 (*Affiliations Schedule*): subsidiary taxpayer identity information, annual accounting period, subsidiary PBA code, parent taxpayer identity information, parent PBA code, Master File Tax Code, Document Locator Number, and cycle posted. As a result, these items of return information currently listed in §301.6103(j)(5)–1 will be removed by this document.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and because no preceding notice of proposed rulemaking is required for this temporary regulation, the provisions of the Regulatory Flexibility Act (5 U.S.C. chapter 6) do not apply. Pursuant to section 7805(f) of the Code, the IRS will submit this Treasury decision to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Drafting Information

The principal author of these regulations is Christine Irwin, Office of the As-

sociate Chief Counsel, Procedure & Administration (Disclosure & Privacy Law Division).

* * * * *

Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 301 is amended as follows:

PART 301—PROCEDURE AND ADMINISTRATION

Paragraph 1. The authority citation for part 301 is amended by removing the entry for “Section 301.6103(j)(5)–1” and adding an entry in numerical order to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

Section 301.6103(j)(5)–1T also issued under 26 U.S.C. 6103(j)(5). * * *

§301.6103(j)(5)–1 [Removed]

Par. 2. Section 301.6103(j)(5)–1 is removed.

Par. 3. Section 301.6103(j)(5)–1T is added to read as follows:

§301.6103(j)(5)–1T Disclosures of return information reflected on returns to officers and employees of the Department of Agriculture for conducting the census of agriculture (temporary).

(a) *General rule.* Pursuant to the provisions of section 6103(j)(5) of the Internal Revenue Code and subject to the requirements of paragraph (c) of this section, officers or employees of the Internal Revenue Service will disclose return information reflected on returns to officers and employees of the Department of Agriculture to the extent, and for such purposes, as may be provided by paragraph (b) of this section. “Return information reflected on returns” includes, but is not limited to, information on returns, information derived from processing such returns, and information derived from other sources for the purposes of establishing and maintaining taxpayer information relating to returns.

(b) *Disclosure of return information reflected on returns to officers and employees of the Department of Agriculture.* (1) Officers or employees of the Internal Revenue Service will disclose the following return information reflected on returns in this

paragraph (b) for individuals, partnerships and corporations with agricultural activity, as determined generally by industry code classification or the filing of returns for such activity, to officers and employees of the Department of Agriculture for purposes of, but only to the extent necessary in, structuring, preparing, and conducting, as authorized by chapter 55 of title 7, United States Code, the census of agriculture.

(2) From Form 1040 (Schedule F)—

(i) Taxpayer identity information (as defined in section 6103(b)(6) of the Internal Revenue Code);

(ii) Spouse's Social Security Number;

(iii) Annual accounting period;

(iv) Principal Business Activity (PBA) code;

(v) Taxable cooperative distributions;

(vi) Income from custom hire and machine work;

(vii) Gross income;

(viii) Master File Tax (MFT) code;

(ix) Document Locator Number (DLN);

(x) Cycle posted;

(xi) Final return indicator;

(xii) Part year return indicator; and

(xiii) Taxpayer telephone number.

(3) From Form 943—

(i) Taxpayer identity information;

(ii) Annual accounting period;

(iii) Total wages subject to Medicare taxes;

(iv) MFT code;

(v) DLN;

(vi) Cycle posted;

(vii) Final return indicator; and

(viii) Part year return indicator.

(4) From Form 1120 series —

(i) Taxpayer identity information;

(ii) Annual accounting period;

(iii) Gross receipts less returns and allowances;

(iv) PBA code;

(v) MFT Code;

(vi) DLN;

(vii) Cycle posted;

(viii) Final return indicator;

(ix) Part year return indicator; and

(x) Consolidated return indicator.

(5) From Form 1065 series —

(i) Taxpayer identity information;

(ii) Annual accounting period;

(iii) PBA code;

(iv) Gross receipts less returns and allowances;

(v) Net farm profit (loss);

(vi) MFT code;

- (vii) DLN;
- (viii) Cycle posted;
- (ix) Final return indicator; and
- (x) Part year return indicator.

(c) *Procedures and Restrictions.* (1) Disclosure of return information reflected on returns by officers or employees of the Internal Revenue Service as provided by paragraph (b) of this section will be made only upon written request designating, by name and title, the officers and employees of the Department of Agriculture to whom such disclosure is authorized, to the Commissioner of Internal Revenue by the Secretary of Agriculture and describing—

- (i) The particular return information reflected on returns for disclosure;
- (ii) The taxable period or date to which such return information reflected on returns relates; and
- (iii) The particular purpose for the requested return information reflected on returns.

(2) (i) No such officer or employee to whom the Internal Revenue Service discloses return information reflected on returns pursuant to the provisions of paragraph (b) of this section shall disclose such information to any person, other than the taxpayer to whom such return information reflected on returns relates or other officers or employees of the Department of Agriculture whose duties or responsibilities require such disclosure for a purpose described in paragraph (b) of this section, except in a form that cannot be associated with, or otherwise identify, directly or indirectly, a particular taxpayer.

(ii) If the Internal Revenue Service determines that the Department of Agriculture, or any officer or employee thereof, has failed to, or does not, satisfy the requirements of section 6103(p)(4) of the Internal Revenue Code or regulations or published procedures thereunder, the Internal Revenue Service may take such actions as are deemed necessary to ensure that such requirements are or shall be satisfied, including suspension of disclosures of return information reflected on returns otherwise authorized by section 6103(j)(5) and paragraph (b) of this section, until the Internal Revenue Service determines that such requirements have been or will be satisfied.

(d) *Effective date.* This section is applicable on June 6, 2003.

David A. Mader,
*Assistant Deputy Commissioner of
Internal Revenue.*

Approved May 12, 2003.

Pamela F. Olson,
*Assistant Secretary of the Treasury
(Tax Policy).*

(Filed by the Office of the Federal Register on June 5, 2003, 8:45 a.m., and published in the issue of the Federal Register for June 6, 2003, 68 F.R. 33857)

Section 6231(a)(1)(B).—Definitions and Special Rules — Exception for Small Partnerships

26 CFR 1.6231(a)(1)–1: Exception for small partnerships.

Small partnership exception. This ruling addresses the issue of whether a partnership qualifies for the small partnership exception provided in section 6231(a)(1)(B) of the Code, and thus does not fall within the unified audit and litigation procedures under sections 6221 through 6234 (TEFRA partnership provisions), where one of the partners is either an organization that is exempt from taxation under section 501(a) that meets the definition of a C corporation for federal tax purposes or a foreign corporation.

Rev. Rul. 2003–69

ISSUE:

Whether a partnership qualifies for the small partnership exception provided in I.R.C. § 6231(a)(1)(B), and thus does not fall within the unified audit and litigation procedures under sections 6221 through 6234 (TEFRA partnership provisions), where one of the partners is either an organization that is exempt from taxation under section 501(a) that meets the definition of a C corporation for federal tax purposes or a foreign corporation.

FACTS:

Situation 1. Partnership A (a domestic partnership required to file returns pursuant to section 6031(a)) consists of three partners, X, Y, and Z. X is an individual and U.S. citizen, Y is a domestic C corporation, and Z is an association that is ex-

empt from taxation under section 501(a). Z also meets the definition of a C corporation for federal tax purposes.

Situation 2. Partnership B (a domestic partnership required to file returns pursuant to section 6031(a)) consists of three partners, U, V, and W. U is an individual and U.S. citizen, V is a domestic C corporation, and W is a foreign corporation.

LAW AND ANALYSIS:

Section 6231 defines a partnership item as an item required to be taken into account for the partnership's taxable year under subtitle A, to the extent regulations provide that the item is more appropriately determined at the partnership level than at the partner level. Under section 6221, the tax treatment of any partnership item shall be determined at the partnership level under the TEFRA partnership provisions. As a general rule, the TEFRA partnership provisions apply to any partnership required to file a return of partnership income under section 6031. Section 6231(a)(1)(A). The TEFRA partnership provisions, however, do not apply to a partnership that qualifies as a small partnership under section 6231(a)(1)(B), unless the partnership elects to apply those provisions.

For taxable years ending after August 5, 1997, section 6231(a)(1)(B) defines a small partnership as a partnership in which there are ten or fewer partners each of whom is an individual (other than a nonresident alien), an estate of a deceased partner, or a C corporation. Treas. Reg. § 301.6231(a)(1)–1, which is effective for partnership taxable years beginning on or after October 4, 2001, addresses the exception for small partnerships and refers to section 1361(a)(2) for the definition of C corporation. Section 1361(a)(2) provides that “for purposes of [the Internal Revenue Code], the term ‘C corporation’ means, with respect to any taxable year, a corporation which is not an S corporation for such year.”

Section 7701(a)(3) defines the term corporation as including “associations, joint-stock companies, and insurance companies.” Treas. Reg. § 301.7701–2(b) states that the term corporation means: (1) a business entity organized under federal or state statute (or under a statute of a federally recognized Indian tribe) if the statute refers to the entity as incorporated or as a corporation, body corporate, or body politic; (2) an

association (determined under section 301.7701-3); (3) a business entity organized under state statute, if the statute refers to the entity as a joint-stock company or joint-stock association; (4) an insurance company; (5) a state-chartered business entity conducting banking activities, if any of its deposits are insured under the Federal Deposit Insurance Act (12 U.S.C. § 1811 *et seq.*), or a similar federal statute; (6) a business entity wholly owned by a state or any political subdivision thereof; (7) a business entity that is taxable as a corporation under a provision of the Internal Revenue Code other than section 7701(a)(3); and (8) certain foreign entities.

Treas. Reg. § 301.7701-3 allows a business entity that is not classified as a corporation under Treas. Reg. § 301.7701-2(b)(1), (3), (4), (5), (6), (7), or (8) (an eligible entity) to elect its classification for federal tax purposes. Under Treas. Reg. § 301.7701-3(c)(1)(v), an eligible entity that is determined to be, or claims to be, exempt from tax under section 501(a) is treated as having made an election to be classified as a corporation.

As a general matter, an S corporation is defined in section 1361(a) as a “small business corporation.” A “small business corporation” is defined by section 1361(b), in part, as “a domestic corporation.” Treas. Reg. § 301.7701-5 defines a domestic corporation as one organized or created in the United States and a foreign corporation as one that is not domestic.

Thus, an exempt organization under section 501(a) can be a “C corporation” for purposes of the small partnership exception. Similarly, because a foreign corporation cannot be an S corporation, the corporation is a C corporation for purposes of the small partnership exception.

Accordingly, in each of the situations described above, all of the partners in the respective partnerships are either individuals (other than a nonresident alien) or C corporations.

HOLDINGS:

Situation 1. Partnership A qualifies for the small partnership exception to the TEFRA partnership provisions.

Situation 2. Partnership B qualifies for the small partnership exception to the TEFRA partnership provisions.

DRAFTING INFORMATION

The principal author of this revenue ruling is David A. Abernathy of the Office of Associate Chief Counsel (Procedure and Administration), Administrative Provisions and Judicial Practice Division. For further information regarding this revenue ruling, contact Mr. Abernathy at (202) 622-7940 (not a toll-free call).

Section 7805.—Rules and Regulations

26 CFR 301.7805-1: Rules and Regulations.

Obsolete revenue rulings. This ruling

obsoletes prior rulings which have been identified as no longer being determinative.

Rev. Rul. 2003-67

The Internal Revenue Service is continuing its program of reviewing rulings (including revenue rulings, revenue procedures and notices) published in the Internal Revenue Bulletin to identify and publish lists of those rulings that, although not specifically revoked or superseded, are no longer considered determinative because: (1) the applicable statutory provisions or regulations have been changed or repealed; (2) the ruling position is specifically covered by statute, regulations, or subsequent published position; or, (3) the facts set forth no longer exist or are not sufficiently described to permit clear application of the current statute and regulations.

This revenue ruling publishes a list of rulings that have been identified under the Service’s review program as no longer being determinative. The rulings are categorized by the Assistant Chief Counsel offices in the Office of Associate Chief Counsel (Procedure and Administration) that have primary jurisdiction over the subject matter of the rulings that have been identified as no longer being determinative.

Accordingly, the rulings listed below are hereby declared obsolete.

Assistant Chief Counsel (Administrative Provisions and Judicial Practice)

<i>Ruling No.</i>	<i>C.B. Citation</i>
Rev. Rul. 54-86	1954-1 C.B. 79
Rev. Rul. 54-431	1954-2 C.B. 116
Rev. Rul. 54-571	1954-2 C.B. 235
Rev. Rul. 55-606	1955-2 C.B. 489
Rev. Rul. 59-328	1959-2 C.B. 379
Rev. Rul. 63-248	1963-2 C.B. 623
Rev. Rul. 64-36	1964-1 C.B. 446
Rev. Rul. 65-129	1965-1 C.B. 519
Rev. Rul. 65-248	1965-2 C.B. 432
Rev. Rul. 66-270	1966-2 C.B. 106
Rev. Rul. 67-121	1967-1 C.B. 363
Rev. Rul. 67-197	1967-1 C.B. 319
Rev. Rul. 71-310	1971-2 C.B. 169
Rev. Rul. 73-232	1973-1 C.B. 541
Rev. Rul. 74-126	1974-1 C.B. 337

<i>Ruling No.</i>	<i>C.B. Citation</i>
Rev. Rul. 76-561	1976-2 C.B. 395
Rev. Rul. 77-53	1977-1 C.B. 368
Rev. Rul. 78-157	1978-1 C.B. 431
Rev. Rul. 78-169	1978-1 C.B. 432
Rev. Rul. 81-245	1981-2 C.B. 235
Rev. Rul. 85-37	1985-1 C.B. 362
Rev. Rul. 85-50	1985-1 C.B. 345
Rev. Proc. 88-16	1988-1 C.B. 691
Rev. Rul. 93-70	1993-2 C.B. 294

Assistant Chief Counsel (Collection, Bankruptcy and Summons)

<i>Ruling No.</i>	<i>Citation</i>
Rev. Rul. 225 (1953)	1953-2 C.B. 467
Rev. Rul. 54-93	1954-1 C.B. 280
Rev. Rul. 54-125	1954-1 C.B. 282
Rev. Rul. 55-134	1955-1 C.B. 196
Rev. Rul. 55-227	1955-1 C.B. 551
Rev. Rul. 56-41	1956-1 C.B. 562
Rev. Rul. 66-383	1966-2 C.B. 502
Rev. Proc. 67-25	1967-1 C.B. 626
Rev. Proc. 71-37	1971-2 C.B. 573
Rev. Proc. 76-23	1976-1 C.B. 562

Assistant Chief Counsel (Disclosure and Privacy Law)

<i>Ruling No.</i>	<i>Citation</i>
Rev. Rul. 54-598	1954-2 C.B. 121
Rev. Proc. 58-120	1958-1 C.B. 498
Rev. Proc. 66-4	1966-1 C.B. 607
Rev. Proc. 70-11	1970-1 C.B. 437
Rev. Proc. 73-6	1973-1 C.B. 752
Rev. Proc. 85-21	1985-1 C.B. 539
Rev. Proc. 85-33	1985-2 C.B. 414
Rev. Proc. 88-39	1988-2 C.B. 562
Rev. Proc. 89-33	1989-1 C.B. 905
Rev. Proc. 91-42	1991-2 C.B. 717
Rev. Proc. 92-55	1992-2 C.B. 394

The Service will continue to review other rulings to identify those that, for the reasons stated above, are no longer determinative. Therefore, failure to include any particular ruling in the above list should not be construed as an indication that the ruling necessarily is determinative.

DRAFTING INFORMATION

The principal author of this revenue ruling is A. M. Gulas of the Office of Associate Chief Counsel, Procedure and Administration (Disclosure and Privacy Law).

For further information regarding the rulings obsoleted in this revenue ruling, contact the following persons from the appropriate Assistant Chief Counsel offices (not toll-free calls):

<i>Name</i>	<i>Assistant Chief Counsel</i>	<i>Telephone No.</i>
Blaise Dusenberry	Administrative Provisions & Judicial Practice	202-622-7940
Peter Devlin	Collection, Bankruptcy & Summons	202-622-3600
A. M. Gulas	Disclosure & Privacy Law	202-622-4560

Part III. Administrative, Procedural, and Miscellaneous

Notice of Proposed Revenue Procedure for Cardholder/Payors to Rely on Merchant Category Codes to Determine Reportable Payments

Notice 2003-37

This notice provides a proposed revenue procedure that, when finalized, would provide an optional procedure that payors and their authorized agents may use in determining whether payment card transactions are reportable under section 6041 or section 6041A of the Internal Revenue Code.

The Internal Revenue Service requests comments on this proposed revenue procedure. Written comments must be received by September 29, 2003. Comments should be submitted to: CC:PA:RU (NOT-129380-02), Room 5526, Internal Revenue Service, Ben Franklin Station, Washington, DC 20224. Alternatively, comments may be hand delivered between the hours of 8:00 a.m. and 5:00 p.m. to CC:PA:RU (NOT-129380-02), Courier's Desk, Internal Revenue Service, 1111 Constitution Ave., NW, Washington, DC. Comments may also be transmitted electronically via the following e-mail address: *Notice.Comments@irs.counsel.treas.gov*. Please include "Notice 2003-37" in the subject line of any electronic communications.

For further information regarding this notice, contact Joseph P. Dewald of the Office of Associate Chief Counsel (Procedure and Administration), Administrative Provisions and Judicial Practice Division. Mr. Dewald may be contacted at 202-622-4910 (not a toll-free call).

APPENDIX (PROPOSED REVENUE PROCEDURE)

SECTION 1. PURPOSE

This revenue procedure provides an optional procedure that payors may use in determining whether payment card transactions are reportable under section 6041 or section 6041A of the Internal Revenue Code. In addition, payors, or their authorized agents, may use this optional procedure

in determining whether payment card transactions are reportable payments for purposes of the Internal Revenue Service TIN Matching Program under section 3406.

In general, this revenue procedure classifies businesses, by Merchant Category Codes (MCCs), according to whether they predominantly furnish services (for which payments are reportable) or predominantly provide goods (for which payments are not reportable). A payment card organization or one of its members or affiliates may assign MCCs, or equivalent Industry Codes, to merchant/payees that accept its payment cards and notify cardholder/payors that use its payment card of the MCC or equivalent Industry Code assigned to a merchant/payee. A cardholder/payor may then rely on the MCC or equivalent Industry Code assigned to a merchant/payee in determining whether a payment card transaction with that merchant/payee is subject to reporting under section 6041 or section 6041A.

SECTION 2. BACKGROUND

.01 *Reporting requirements under sections 6041 and 6041A.* If a person is engaged in a trade or business and, in the course of that trade or business, pays any person \$600 or more of rent, salaries, wages, premiums, annuities, compensation, remunerations, emoluments, or other fixed or determinable gains, profits, and income during a calendar year, section 6041 generally requires the payor to file an information return with the Internal Revenue Service and to furnish an information statement to the payee.

Section 1.6041-3(c) of the Income Tax Regulations provides an exception to reporting for payments for merchandise, telegrams, telephone, freight, storage and similar charges. Section 1.6041-3(p)(1) provides an exception to reporting for payments made to a corporation, unless the corporation is engaged in providing medical and health care services or is engaged in the billing and collecting of payments in respect to providing medical and health care services. The same provision also provides that reporting is not required for payments made to a hospital or extended care facility that is a tax-exempt organization described in section 501(c)(3) or to a hospital or extended care facility owned and operated by the United States, a State, the District of Co-

lumbia, a possession of the United States, or a political subdivision, agency or instrumentality of any of the foregoing. Section 1.6041-3(p)(2) provides that reporting is not required for payments to an organization exempt from taxation under section 501(a) or an individual retirement plan. Section 1.6041-3(p)(3) provides that reporting is not required for payments made to the United States. Section 1.6041-3(p)(4) provides that reporting is not required for payments made to a State, the District of Columbia, a possession of the United States, or any political subdivision of the foregoing.

If a person is engaged in a trade or business and, in the course of that trade or business, pays any person \$600 or more for services during a calendar year, section 6041A(a) generally requires the payor to file an information return with the Service and to furnish an information statement to the service provider. In general, the exceptions to reporting under section 6041 apply to reporting under section 6041A. However, section 6041A(d)(3) provides that reporting is generally required for payments made by a federal executive agency to a corporation.

Revenue Ruling 81-232, 1981-2 C.B. 231, involved an insurance company making payments to an automobile repair shop for the repair of an insured automobile. The repair contract required payment of \$300 for labor and \$700 for parts. The ruling held that the entire payment was reportable under section 6041 because the portion of the payment attributable to parts was merely incidental to the obligation to repair the automobile. The ruling further held that no part of the payment was excepted from the reporting requirements of section 6041 as a payment of a bill for merchandise.

.02 *Payment card transactions.* A payment card transaction is a transaction in which a cardholder/payor uses a payment card (as defined in section 4.05 of this revenue procedure) to purchase goods or services and a merchant agrees to accept a payment card as a means of obtaining payment. A payment card organization (as defined in section 4.06 of this revenue procedure) sets the standards and provides the mechanism, either directly or indirectly through members and affiliates, for effecting the payment.

Payment card organizations and the Information Reporting Program Advisory Committee have recommended that cardholder/payors be allowed to rely on MCCs or equivalent Industry Codes provided by the payment card organization in determining, for purposes of sections 6041 and 6041A(a), whether a payment card transaction is a payment for services or a payment for goods.

SECTION 3. SCOPE.

This revenue procedure applies to payment card organizations and their members and affiliates and to cardholder/payors that purchase goods or services in payment card transactions. In addition, cardholder/payors, or their authorized agents, will be allowed to rely on MCCs or equivalent Industry Codes for purposes of TIN matching with respect to reportable payments.

SECTION 4. DEFINITIONS

For purposes of this revenue procedure, the terms listed below are defined as follows:

.01 *Cardholder*. A cardholder is the payor for payments made to a merchant/payee through a payment card.

.02 *Merchant*. A merchant is a payee that has entered into an agreement with a payment card organization, or a member or affiliate, to accept the organization's payment card as payment for goods and services.

.03 *Merchant Category Code*. A Merchant Category Code (MCC) is a classification code that is assigned by a payment card organization or one of its members or affiliates to a merchant that has been accepted to participate in the payment card system as a card-accepting merchant. The payment card organization or one of its members or affiliates assigns the merchant a particular code based on the predominant business activity of the merchant.

.04 *Industry Code*. An Industry Code is the number that corresponds to, and identifies, a merchant in the same business as a merchant assigned a particular MCC.

.05 *Payment Card*. A payment card is a card (or an account) issued by a payment card organization, or one of its members or affiliates, to a cardholder/payor, which upon presentation to a merchant/payee, represents an agreement of the cardholder to pay the merchant through the payment card organization.

.06 *Payment Card Organization*. A payment card organization is an entity that sets the standards and provides the mechanism, either directly or indirectly through members and affiliates, for effectuating payment between a purchaser and a merchant in a payment card transaction. A payment card organization generally provides such a payment mechanism by issuing payment cards, enrolling merchants as authorized acceptors of payment cards for payment for goods or services, and ensuring the system conducts the transactions in accordance with prescribed standards.

.07 *Payment Card Transactions*. A payment card transaction is a transaction in which a cardholder/payor uses a payment card (as defined in section 4.05 of this revenue procedure) to purchase goods or services, and a merchant agrees to accept a payment card as a means of obtaining payment.

SECTION 5. APPLICATION

.01 *Payment Card Organizations*. A payment card organization or one of its members or affiliates may assign MCCs, or equivalent Industry Codes, to merchant/payees that accept its payment cards and notify cardholder/payors that use its payment card of the MCC or equivalent Industry Code assigned to a merchant/payee. The MCCs assigned to merchant/payees must be determined under the table in section 5.03 of this revenue procedure. If the Internal Revenue Service notifies the

payment card organization that the MCC or equivalent Industry Code assigned to a merchant/payee is incorrect, this revenue procedure does not apply to a payment card transaction with the merchant/payee occurring after the date of the notification unless the payment card organization or one of its members or affiliates has assigned the merchant/payee a MCC or equivalent Industry Code that is satisfactory to the Internal Revenue Service and has notified the cardholder/payor of the correction.

.02 *Cardholder/payors*. A cardholder/payor may rely on the MCC or equivalent Industry Code assigned to a merchant/payee in determining whether a payment card transaction with that merchant/payee is subject to information reporting under section 6041 or section 6041A. Thus, if a merchant/payee is assigned a MCC and the table in section 5.03 indicates that payments to merchants in that category are not reportable under section 6041 or section 6041A, a cardholder/payor is not required to report payment card transactions with the merchant/payee. Similarly, an indication in the table that payments to a category of merchants are reportable under section 6041 or section 6041A reflects a determination by the Internal Revenue Service that those merchants predominantly furnish services, and cardholder/payors may treat payment card transactions with those merchants as payments for services. Although the transactions do not qualify for the merchandise exception to information reporting under this revenue procedure, they may qualify for the exception under the generally applicable rules of sections 6041 and 6041A if, in fact, only merchandise is provided. In addition, other exceptions to information reporting (such as the exception for payments to corporations) may apply.

.03 *Table*. The following table is used in applying the optional procedure permitted under this revenue procedure.

MCC	Merchant	Reportable under 6041/6041A and Authority for Exception
0742	Veterinary Services	Yes
0763	Agricultural Cooperative	Yes
0780	Landscaping Services	Yes
1520	General Contractors	Yes
1711	Heating, Plumbing, A/C	Yes
1731	Electrical Contractors	Yes
1740	Masonry, Stonework, and Plaster	Yes
1750	Carpentry Contractors	Yes
1761	Roofing/Siding, Sheet Metal	Yes
1771	Concrete Work Contractors	Yes
1799	Special Trade Contractors	Yes
2741	Miscellaneous Publishing and Printing	Yes
2791	Typesetting, Plate Making, and Related Services	Yes
2842	Specialty Cleaning	Yes
3000–3299	Airlines	Yes
3351–3441	Car Rental	Yes
3501–3790	Hotels/Motels/Inns/Resorts	Yes
4011	Railroads	No 1.6041–3(c)
4111	Commuter Transport, Ferries	Yes
4112	Passenger Railways	Yes
4119	Ambulance Services	Yes
4121	Taxicabs/Limousines	Yes
4131	Bus Lines	Yes
4214	Motor Freight Carriers and Trucking - Local and Long Distance, Moving and Storage Companies, and Local Delivery Services	No 1.6041–3(c)
4215	Courier Services	Yes
4225	Public Warehousing and Storage - Farm Products, Refrigerated Goods, Household Goods, and Storage	No 1.6041–3(c)
4411	Cruise Lines	Yes
4457	Boat Rentals and Leases	Yes
4468	Marinas, Service and Supplies	Yes
4511	Airlines, Air Carriers	Yes
4582	Airports, Flying Fields	Yes
4722	Travel Agencies, Tour Operators	Yes
4723	TUI Travel - Germany	Yes
4784	Tolls/Bridge Fees	No 1.6041–3(c)
4789	Transportation Services (Not Elsewhere Classified)	Yes
4812	Telecommunication Equipment and Telephone Sales	No 1.6041–3(c)
4814	Telecommunication Services	No 1.6041–3(c)
4815	Visaphone	No 1.6041–3(c)
4816	Computer Network Services	No 1.6041–3(c)
4821	Telegraph Services	No 1.6041–3(c)

MCC	Merchant	Reportable under 6041/6041A and Authority for Exception
4829	Wires, Money Orders	No 1.6041-3(c)
4899	Cable, Satellite, and Other Pay Television and Radio	No 1.6041-3(c)
4900	Utilities	No 1.6041-3(c)
5013	Motor Vehicle Supplies and New Parts	No 1.6041-3(c)
5021	Office and Commercial Furniture	No 1.6041-3(c)
5039	Construction Materials (Not Elsewhere Classified)	No 1.6041-3(c)
5044	Photographic, Photocopy, Microfilm Equipment, and Supplies	No 1.6041-3(c)
5045	Computers, Peripherals, and Software	No 1.6041-3(c)
5046	Commercial Equipment (Not Elsewhere Classified)	No 1.6041-3(c)
5047	Medical, Dental, Ophthalmic, and Hospital Equipment and Supplies	No 1.6041-3(c)
5051	Metal Service Centers	No 1.6041-3(c)
5065	Electrical Parts and Equipment	No 1.6041-3(c)
5072	Hardware, Equipment, and Supplies	No 1.6041-3(c)
5074	Plumbing, Heating Equipment, and Supplies	No 1.6041-3(c)
5085	Industrial Supplies (Not Elsewhere Classified)	No 1.6041-3(c)
5094	Precious Stones and Metals, Watches and Jewelry	No 1.6041-3(c)
5099	Durable Goods (Not Elsewhere Classified)	No 1.6041-3(c)
5111	Stationary, Office Supplies, Printing and Writing Paper	No 1.6041-3(c)
5122	Drugs, Drug Proprietaries, and Druggist Sundries	No 1.6041-3(c)
5131	Piece Goods, Notions, and Other Dry Goods	No 1.6041-3(c)
5137	Uniforms, Commercial Clothing	No 1.6041-3(c)
5139	Commercial Footwear	No 1.6041-3(c)
5169	Chemicals and Allied Products (Not Elsewhere Classified)	No 1.6041-3(c)
5172	Petroleum and Petroleum Products	No 1.6041-3(c)
5192	Books, Periodicals, and Newspapers	No 1.6041-3(c)
5193	Florists Supplies, Nursery Stock, and Flowers	No 1.6041-3(c)

MCC	Merchant	Reportable under 6041/6041A and Authority for Exception
5198	Paints, Varnishes, and Supplies	No 1.6041-3(c)
5199	Nondurable Goods (Not Elsewhere Classified)	No 1.6041-3(c)
5200	Home Supply Warehouse Stores	No 1.6041-3(c)
5211	Lumber, Building Materials Stores	No 1.6041-3(c)
5231	Glass, Paint, and Wallpaper Stores	No 1.6041-3(c)
5251	Hardware Stores	No 1.6041-3(c)
5261	Nurseries, Lawn and Garden Supply Stores	No 1.6041-3(c)
5271	Mobile Home Dealers	No 1.6041-3(c)
5300	Wholesale Clubs	No 1.6041-3(c)
5309	Duty Free Stores	No 1.6041-3(c)
5310	Discount Stores	No 1.6041-3(c)
5311	Department Stores	No 1.6041-3(c)
5331	Variety Stores	No 1.6041-3(c)
5399	Miscellaneous General Merchandise	No 1.6041-3(c)
5411	Grocery Stores, Supermarkets	No 1.6041-3(c)
5422	Freezer and Locker Meat Provisioners	No 1.6041-3(c)
5441	Candy, Nut, and Confectionery Stores	No 1.6041-3(c)
5451	Dairy Products Stores	No 1.6041-3(c)
5462	Bakeries	No 1.6041-3(c)
5499	Miscellaneous Food Stores - Convenience Stores and Specialty Markets	No 1.6041-3(c)
5511	Auto Service, Repairs	Yes
5521	Auto/Truck Dealers	No 1.6041-3(c)
5531	Auto and Home Supply Stores	No 1.6041-3(c)
5532	Automotive Tire Stores	No 1.6041-3(c)
5533	Automotive Parts and Accessories Stores	No 1.6041-3(c)
5541	Service Stations	No 1.6041-3(c)

MCC	Merchant	Reportable under 6041/6041A and Authority for Exception
5542	Automated Fuel Dispensers	No 1.6041-3(c)
5551	Boat Dealers	No 1.6041-3(c)
5561	Motorcycle Shops, Dealers	No 1.6041-3(c)
5571	Motorcycle Shops and Dealers	No 1.6041-3(c)
5592	Motor Homes Dealers	No 1.6041-3(c)
5598	Snowmobile Dealers	No 1.6041-3(c)
5599	Miscellaneous Auto Dealers	No 1.6041-3(c)
5611	Men's and Boy's Clothing and Accessories Stores	No 1.6041-3(c)
5621	Women's Ready-To-Wear Stores	No 1.6041-3(c)
5631	Women's Accessory and Specialty Shops	No 1.6041-3(c)
5641	Children's and Infant's Wear Stores	No 1.6041-3(c)
5651	Family Clothing Stores	No 1.6041-3(c)
5655	Sports and Riding Apparel Stores	No 1.6041-3(c)
5661	Shoe Stores	No 1.6041-3(c)
5681	Furriers and Fur Shops	No 1.6041-3(c)
5691	Men's, Women's Clothing Stores	No 1.6041-3(c)
5697	Tailors, Alterations	Yes
5698	Wig and Toupee Stores	No 1.6041-3(c)
5699	Miscellaneous Apparel and Accessory Shops	No 1.6041-3(c)
5712	Furniture, Home Furnishings, and Equipment Stores, Except Appliances	No 1.6041-3(c)
5713	Floor Covering Stores	No 1.6041-3(c)
5714	Drapery, Window Covering, and Upholstery Stores	No 1.6041-3(c)
5718	Fireplace, Fireplace Screens, and Accessories Stores	No 1.6041-3(c)
5719	Miscellaneous Home Furnishing Specialty Stores	No 1.6041-3(c)
5722	Household Appliance Stores	No 1.6041-3(c)
5732	Electronics Stores	No 1.6041-3(c)

MCC	Merchant	Reportable under 6041/6041A and Authority for Exception
5733	Music Stores-Musical Instruments, Pianos, and Sheet Music	No 1.6041-3(c)
5734	Computer Software Stores	No 1.6041-3(c)
5735	Record Stores	No 1.6041-3(c)
5811	Caterers	Yes
5812	Eating Places, Restaurants	No 1.6041-3(c)
5813	Drinking Places	No 1.6041-3(c)
5814	Fast Food Restaurants	No 1.6041-3(c)
5912	Drug Stores and Pharmacies	No 1.6041-3(c)
5921	Package Stores-Beer, Wine, and Liquor	No 1.6041-3(c)
5931	Used Merchandise and Secondhand Stores	No 1.6041-3(c)
5932	Antique Shops	No 1.6041-3(c)
5933	Pawn Shops	No 1.6041-3(c)
5935	Wrecking and Salvage Yards	Yes
5937	Antique Reproductions	No 1.6041-3(c)
5940	Bicycle Shops	No 1.6041-3(c)
5941	Sporting Goods Stores	No 1.6041-3(c)
5942	Book Stores	No 1.6041-3(c)
5943	Stationery Stores, Office, and School Supply Stores	No 1.6041-3(c)
5944	Jewelry Stores, Watches, Clocks, and Silverware Stores	No 1.6041-3(c)
5945	Hobby, Toy, and Game Shops	No 1.6041-3(c)
5946	Camera and Photographic Supply Stores	No 1.6041-3(c)
5947	Gift, Card, Novelty, and Souvenir Shops	No 1.6041-3(c)
5948	Luggage and Leather Goods Stores	No 1.6041-3(c)
5949	Sewing, Needlework, Fabric, and Piece Goods Stores	No 1.6041-3(c)
5950	Glassware, Crystal Stores	No 1.6041-3(c)
5960	Direct Marketing - Insurance Services	Yes
5962	Direct Marketing - Travel	Yes
5963	Door-To-Door Sales	No 1.6041-3(c)

MCC	Merchant	Reportable under 6041/6041A and Authority for Exception
5964	Direct Marketing - Catalog Merchant	No 1.6041-3(c)
5965	Direct Marketing - Combination Catalog and Retail Merchant	No 1.6041-3(c)
5966	Direct Marketing - Outbound Tele	No 1.6041-3(c)
5967	Direct Marketing - Inbound Tele	No 1.6041-3(c)
5968	Direct Marketing - Subscription	No 1.6041-3(c)
5969	Direct Marketing - Other	No 1.6041-3(c)
5970	Artist's Supply and Craft Shops	No 1.6041-3(c)
5971	Art Dealers and Galleries	No 1.6041-3(c)
5972	Stamp and Coin Stores	No 1.6041-3(c)
5973	Religious Goods Stores	No 1.6041-3(c)
5975	Hearing Aids Sales and Supplies	No 1.6041-3(c)
5976	Orthopedic Goods - Prosthetic Devices	No 1.6041-3(c)
5977	Cosmetic Stores	No 1.6041-3(c)
5978	Typewriter Stores	No 1.6041-3(c)
5983	Fuel Dealers (Non Automotive)	No 1.6041-3(c)
5992	Florists	No 1.6041-3(c)
5993	Cigar Stores and Stands	No 1.6041-3(c)
5994	News Dealers and Newsstands	No 1.6041-3(c)
5995	Pet Shops, Pet Food, and Supplies	No 1.6041-3(c)
5996	Swimming Pools Sales	No 1.6041-3(c)
5997	Electric Razor Stores	No 1.6041-3(c)
5998	Tent and Awning Shops	No 1.6041-3(c)
5999	Miscellaneous Specialty Retail	No 1.6041-3(c)
6010	Manual Cash Disburse	No 1.6041-3(c)
6011	Automated Cash Disburse	No 1.6041-3(c)
6012	Financial Institutions	Yes

MCC	Merchant	Reportable under 6041/6041A and Authority for Exception
6051	Non-FI, Money Orders	No 1.6041-3(c)
6211	Security Brokers/Dealers	Yes
6300	Insurance Underwriting, Premiums	No 1.6041-3(c)
6381	Insurance Premiums	No 1.6041-3(c)
6399	Insurance — Default	No 1.6041-3(c)
6513	Real Estate Agents and Managers - Rentals	Yes
7011	Hotels, Motels, and Resorts	Yes
7012	Timeshares	Yes
7032	Sporting/Recreation Camps	Yes
7033	Trailer Parks, Campgrounds	Yes
7210	Laundry, Cleaning Services	Yes
7211	Laundries	Yes
7216	Dry Cleaners	Yes
7217	Carpet/Upholstery Cleaning	Yes
7221	Photographic Studios	Yes
7230	Barber and Beauty Shops	Yes
7251	Shoe Repair/Hat Cleaning	Yes
7261	Funeral Services, Crematories	Yes
7273	Dating/Escort Services	Yes
7276	Tax Preparation Services	Yes
7277	Counseling Services	Yes
7278	Buying/Shopping Services	Yes
7296	Clothing Rental	Yes
7297	Massage Parlors	Yes
7298	Health and Beauty Spas	Yes
7299	Miscellaneous General Services	Yes
7311	Advertising Services	Yes
7321	Credit Reporting Agencies	Yes
7332	Blueprinting and Photocopying Services	Yes
7333	Commercial Photography	Yes
7338	Quick Copy, Repro, and Blueprint	Yes
7339	Secretarial Support Services	Yes
7342	Exterminating Services	Yes
7349	Cleaning and Maintenance	Yes
7361	Employment/Temp Agencies	Yes
7372	Computer Programming	Yes
7375	Information Retrieval Services	Yes
7379	Computer Repair	Yes
7392	Consulting, Public Relations	Yes
7393	Detective Agencies	Yes
7394	Equipment Rental	Yes
7395	Photo Developing	Yes
7399	Miscellaneous Business Services	Yes
7511	Truck Stop	Yes
7512	Car Rental Agencies	Yes
7513	Truck/Utility Trailer Rentals	Yes

MCC	Merchant	Reportable under 6041/6041A and Authority for Exception
7519	Recreational Vehicle Rentals	Yes
7523	Parking Lots, Garages	Yes
7531	Auto Body Repair Shops	Yes
7534	Tire Retreading and Repair	Yes
7535	Auto Paint Shops	Yes
7538	Auto Service Shops	Yes
7542	Car Washes	Yes
7549	Towing Services	Yes
7622	Electronics Repair Shops	Yes
7623	A/C, Refrigeration Repair	Yes
7629	Small Appliance Repair	Yes
7631	Watch/Jewelry Repair	Yes
7641	Furniture Repair, Refinishing	Yes
7692	Welding Repair	Yes
7699	Miscellaneous Repair Shops	Yes
7829	Picture/Video Production	Yes
7832	Motion Picture Theaters	Yes
7841	Video Tape Rental Stores	Yes
7911	Dance Hall, Studios, Schools	Yes
7922	Theatrical Ticket Agencies	Yes
7929	Bands, Orchestras	Yes
7932	Billiard/Pool Establishments	Yes
7933	Bowling Alleys	Yes
7941	Sports Clubs/Fields	Yes
7991	Tourist Attractions and Exhibits	Yes
7992	Golf Courses - Public	Yes
7993	Video Amusement Game Supplies	No 1.6041-3(c)
7994	Video Game Arcades	Yes
7995	Betting/Casino Gambling	Yes
7996	Amusement Parks/Carnivals	Yes
7997	Country Clubs	Yes
7998	Aquariums	Yes
7999	Miscellaneous Recreation Services	Yes
8011	Doctors	Yes
8021	Dentists, Orthodontists	Yes
8031	Osteopaths	Yes
8041	Chiropractors	Yes
8042	Optometrists, Ophthalmologist	Yes
8043	Opticians, Eyeglasses	Yes
8044	Optical Goods and Glasses	No 1.6041-3(c)
8049	Chiropodists, Podiatrists	Yes
8050	Nursing/Personal Care	Yes
8062	Hospitals	Yes
8071	Medical and Dental Labs	Yes
8099	Medical Services	Yes
8111	Legal Services, Attorneys	Yes
8211	Elementary, Secondary Schools	No 1.6041-3(p)(2)

MCC	Merchant	Reportable under 6041/6041A and Authority for Exception
8220	Colleges, Universities	No 1.6041-3(p)(2)
8241	Correspondence Schools	No 1.6041-3(p)(2)
8244	Business/Secretarial Schools	No 1.6041-3(p)(2)
8249	Vocational/Trade Schools	No 1.6041-3(p)(2)
8299	Educational Services	Yes
8351	Child Care Services	Yes
8398	Charitable and Social Service Organizations - Fundraising	No 1.6041-3(p)(2)
8641	Civic, Social, Fraternal Associations	No 1.6041-3(p)(2)
8651	Political Organizations	Yes
8661	Religious Organizations	No 1.6041-3(p)(2)
8675	Automobile Associations	Yes
8699	Membership Organizations	Yes
8734	Testing Laboratories	Yes
8911	Architectural/Surveying Services	Yes
8931	Accounting/Bookkeeping Services	Yes
8999	Professional Services	Yes
9211	Court Costs, Including Alimony and Child Support - Courts of Law	No 1.6041-3(p)(4)
9222	Fines - Government Administrative Entities	No 1.6041-3(p)(4)
9223	Bail and Bond Payments	Yes
9311	Tax Payments - Government Agencies	No 1.6041-3(p)(4)
9399	Government Services (Not Elsewhere Classified)	No 1.6041-3(p)(4)
9402	Postal Services - Government Only	No 1.6041-3(p)(3)
9405	U.S. Federal Government Agencies or Departments	No 1.6041-3(p)(3)
9950	Intra-Company Purchases	No 1.6041-3(c)

SECTION 5. EFFECTIVE DATE

The procedures are proposed to be effective on the date they are published as a final revenue procedure.

Part IV. Items of General Interest

Notice of Proposed Rulemaking by Cross-Reference to Temporary Regulations

Disclosure of Return Information to the Department of Agriculture

REG-103809-03

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking by cross-reference to temporary regulations.

SUMMARY: The IRS is issuing regulations to incorporate and clarify the phrase "return information reflected on returns" in conformance with the terms of section 6103(j)(5) of the Internal Revenue Code (Code). These temporary regulations also remove certain items of return information that the IRS currently discloses, but the Department of Agriculture no longer needs, for conducting the census of agriculture. The text of the temporary regulations (T.D. 9060) published in this issue of the Bulletin serves as the text of the proposed regulations.

DATES: Written and electronic comments and requests for a public hearing must be received by September 8, 2003.

ADDRESSES: Send submissions to: CC:PA:RU (REG-103809-03), room 5226, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand-delivered between the hours of 8 a.m. and 4 p.m. to CC:PA:RU (REG-103809-03), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC, or sent electronically, via the IRS Internet site at www.irs.gov/reg.

FOR FURTHER INFORMATION CONTACT: Christine Irwin at (202) 622-4570 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

Temporary regulations in this issue of the Bulletin amend the Procedure and Admin-

istration Regulations (26 CFR Part 301) relating to Code section 6103(j)(5). The temporary regulations contain rules relating to the disclosure of return information reflected on returns to officers and employees of the Department of Agriculture for conducting the census of agriculture.

The text of the temporary regulations also serves as the text of these proposed regulations. The preamble to the temporary regulations explains the temporary regulations and these proposed regulations.

Special Analyses

It has been determined this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and because the regulations do not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Code, the IRS will submit this notice of proposed rulemaking to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Comments and Requests for Public Hearing

Before adoption of these proposed regulations as final regulations, the IRS will consider any written (a signed original and eight (8) copies) or electronic comments that the IRS timely receives. The IRS and Treasury Department request comments on the clarity of the proposed rules and how they can be made easier to understand. All comments will be available for public inspection and copying. The IRS may schedule a public hearing if any person who timely submits written comments requests such a hearing in writing. If a public hearing is scheduled, notice of the date, time, and place for the public hearing will be published in the **Federal Register**.

Drafting Information

The principal author of these regulations is Christine Irwin, Office of the Associate Chief Counsel, Procedure & Ad-

ministration (Disclosure & Privacy Law Division).

* * * * *

Proposed Amendments to the Regulations

Accordingly, 26 CFR part 301 is proposed to be amended as follows:

PART 301—PROCEDURE AND ADMINISTRATION

Paragraph 1. The authority citation for part 301 continues to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

Par. 2. Section 301.6103(j)(5)-1 is added to read as follows:

§301.6103(j)(5)-1 Disclosures of return information reflected on returns to officers and employees of the Department of Agriculture for conducting the census of agriculture.

[The text of this proposed section is the same as the text of §301.6103(j)(5)-1T published elsewhere in this issue of the Bulletin.]

David A. Mader,
Assistant Deputy Commissioner of
Internal Revenue.

(Filed by the Office of the Federal Register on June 5, 2003, 8:45 a.m., and published in the issue of the Federal Register for June 6, 2003, 68 F.R. 33887)

Administration of the Earned Income Credit

Announcement 2003-40

I. Purpose

This announcement describes changes the Internal Revenue Service (IRS) is testing in determining qualifying child eligibility under the earned income credit (EIC) under I.R.C. section 32. This announcement also solicits public comment on those changes.

II. Background

The EIC plays a vital role in rewarding work and lifting working families out of poverty. Historically, the EIC program

has experienced a relatively high participation rate. The IRS received claims totaling over \$32 billion from 19 million claimants for tax year 2002. Studies indicate that between 75 and 86 percent of eligible taxpayers participate in the EIC program. In 2001, the EIC lifted 3.9 million people out of poverty.

Although the EIC program has been successful in reaching and assisting low income working families, the EIC program also suffers from high noncompliance. The most recent compliance study, *Compliance Estimates For Earned Income Tax Credit Claimed on 1999 Returns* (the 1999 study), released in February 2002, estimates that out of the \$31.3 billion of EIC claims made by taxpayers for tax year 1999, between \$8.5 and \$9.9 billion — or between 27.0 and 31.7 percent of total EIC claims — were erroneous unrecovered overclaims. The largest amount of EIC overclaims (for which errors were known) was associated with taxpayers claiming children who were not the taxpayers' qualifying children. The most common qualifying child error was claiming a child who did not live with the taxpayer for over half the taxable year and therefore did not satisfy the residency requirement of the EIC. Another common qualifying child error was claiming a child who did not bear an appropriate relationship to the taxpayer. Most taxpayers who did not meet the relationship requirement also did not meet the residency requirement.

EIC noncompliance is high in part because it is difficult for the IRS to verify whether a child claimed by a taxpayer meets the residency and relationship tests of the EIC prior to paying out a refund. The IRS employs extensive outreach and educational programs to inform taxpayers and tax return preparers of the requirements of the EIC. These programs encourage eligible taxpayers to participate in the EIC program and discourage ineligible taxpayers from making erroneous EIC claims. In addition, the IRS conducts examinations to verify the eligibility of individuals with questionable claims. Despite these and other efforts, the IRS has been unable to significantly reduce the noncompliance rate over the years.

To prevent qualifying child errors, the IRS and Treasury Department plan to implement a certification program under which certain taxpayers will be required to demonstrate that they meet the residency re-

quirement with respect to a child before their EIC claims are accepted. The taxpayers required to demonstrate residency will be those who, based on IRS research, are more likely to claim children who do not satisfy the residency requirement (such as caregivers other than the child's parents and fathers who do not file joint returns).

Under the certification program, a taxpayer will be encouraged to fill out a form and provide certain documentation that establishes that the taxpayer meets the residency requirement with respect to a child in advance of the filing season. If such taxpayers choose not to pre-certify, they will be required to send in the same forms and documentation with their tax returns. Taxpayers who pre-certify will receive their EIC refunds faster than taxpayers who send information with their tax returns. Taxpayers who do not pre-certify or send in the required information with their tax returns will be given an additional opportunity to certify residency, after which time, they will be denied the EIC with respect to a claimed child, subject to normal appeals rights and the ability to contest the denial in Tax Court.

The goal of the certification program is to evaluate high-risk EITC claims before they are paid, using a process that is less burdensome to taxpayers and less costly to the IRS than an audit. In addition, the certification program will enable eligible, but high-risk, taxpayers to receive their refunds faster than if they were subsequently challenged by the IRS. By helping to ensure that certain high-risk taxpayers receive the right amount of the credit before refunds are paid, the program will also reduce the burden that is imposed when taxpayers must repay erroneous refunds.

The IRS and the Treasury Department want to implement this program in a manner that will continue the goals of the EIC program, will not be overly burdensome for taxpayers (and other parties) and will not adversely affect participation. Accordingly, the IRS will test the certification program with a limited number of taxpayers (approximately 45,000) and will carefully study the results from this group to determine the effect of certification on compliance and participation. In addition, the IRS and Treasury Department are continuing to evaluate the proposed form and instructions, the types of documentation that will be required, and the IRS' communication and outreach strategy. As part of this evalua-

tion, the IRS will be conducting focus groups of taxpayers, practitioners and third parties (who are asked to help establish residency) prior to the test of the certification program.

As part of the certification program, the IRS and Treasury Department previously considered requiring certain taxpayers whose relationship with a claimed child could not be systematically checked by the IRS through existing databases (*e.g.*, social security records) to establish a qualifying relationship with the child before their EIC claim is accepted. The certification test will not include a relationship certification requirement and will be limited to residency certification.

III. Request for Comments

Based on preliminary discussions and initial drafts of the residency certification form, stakeholders have expressed concerns about various aspects of the certification program. The IRS and Treasury Department are committed to continuing this dialogue with stakeholders and are issuing this announcement to help facilitate comments. Concerns expressed by stakeholders prior to and in response to this announcement will be carefully considered by the IRS and Treasury Department in developing the certification program.

The IRS has revised Form 8836, which is attached to this announcement and will be posted on the IRS' website at <http://www.irs.gov/taxpros/lists/0,,id=97784,00.html>.

The IRS and Treasury Department welcome all comments and suggestions and are particularly interested in comments on the following matters:

1. Under Form 8836, taxpayers will have the option to provide different types of information or documentation to establish residency. Are there other sources or types of information that should be added to the form (as another option) that would still give the IRS reasonable assurances that the taxpayer satisfies the residency requirement? What information or documentation could the IRS request that taxpayers currently possess or could reasonably obtain to verify that the taxpayer resides with a child? What information or documentation currently requested on the forms is difficult or burdensome for the taxpayer or a third party to provide, and why?

2. How can Form 8836 be simplified or clarified? For example, would it be easier for taxpayers to certify one child per form or two children per form? How could the instructions to Form 8836 be simplified or clarified?

3. What can the IRS do to reach out to taxpayers and encourage them to pre-certify, rather than wait until the filing season? What is the message the IRS needs to convey and what are the best means through which to convey that message? Who should be the primary deliverer of particular messages — the IRS or outside stakeholders? Are there other incentives the IRS can provide to taxpayers to encourage them to pre-certify?

4. How can the certification program be used to reach out to taxpayers who are eligible for the EIC, but not currently claim-

ing the credit? Should the messages associated with the certification program be coupled with messages designed to educate taxpayers about their eligibility to claim the EIC and to increase participation? Alternatively, would combining these messages cause confusion, in which case, what separate measures should the IRS take to reach out to eligible taxpayers who are not claiming the credit?

5. What factors should the IRS take into account in designing the study of the initial group of taxpayers who are asked to certify and in evaluating the results of that study?

Comments about the draft Form 8836 or the certification pilot must be submitted on or before July 14, 2003, in order to be considered for the pilot. Otherwise, comments about the precertification process should be

submitted on or before December 31, 2003. Comments about certification taking place during the filing season should be submitted on or before April 15, 2004.

Taxpayers may submit electronic comments on Form 8836 at <http://www.irs.gov/taxpros/lists/0,,id=97784,00.html> and on the pre-certification and certification processes to notice.comments@irscounsel.treas.gov. Alternatively, comments may be sent to: CC:PA:RU (Announcement 2003–40), room 5226, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to: CC:PA:RU (Announcement 2003–40), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC.

Qualifying Children Residency Statement

▶ See instructions starting on page 2.

Part I Taxpayer Information (to be completed by taxpayer)

Your first name and initial	Last name	Your social security number () () ()
If you will be filing a joint return for 2003, spouse's first name and initial	Last name	Spouse's social security number () () ()
Home address (number and street). If you have a P.O. box, see instructions		Your daytime phone number () () () () ()
City, town or post office, state, and ZIP code		Your evening phone number () () () () ()

Part II Qualifying Children Information (to be completed by taxpayer)

Caution. If you have two qualifying children, see instructions before completing this part.

Child 1 ▶	Child's first name	Last name	Child's social security number () () ()
Child 2 ▶	Child's first name	Last name	Child's social security number () () ()

Part III Proof of Residency (to be completed by taxpayer) (see instructions)

Check **one or more** boxes below and attach any required documentation. The combined documentation must include your name, the child's name, street address, and dates the child lived with you to show that you and the child lived together for **more than half** of 2003. See **Residency Test** on page 2 for details and exceptions.

- I have attached copies of one or more of the following official records: Child-care records, community-based organization records, employment records, Indian tribal enrollment records, leases, medical records, religious records, school records, social service agency records, or utility bills.
- I have attached a letter on official letterhead from one or more of the following third parties: Child-care provider, clergy, community-based organization official, employer, health-care provider, Indian tribal official, landlord or property manager, school official, social service agency official, or utility company.
- A third party has completed Part IV below.

Note. The IRS may contact the third party who signs Part IV and any person or organization that provides the documentation you attach to this form.

Under penalties of perjury, I declare that I have examined this statement, and to the best of my knowledge and belief, it is true, correct, and complete.

Taxpayer Sign Here ▶

Signature of spouse
named in Part I ▶

Date ▶

Part IV Third Party Affidavit (to be completed by third party if the last box in Part III is checked)

First, check the box below that best describes your relationship to the taxpayer or one or both children named above.

- Child-care provider Clergy Community-based organization official Employer Health-care provider
- Indian tribal official Landlord or property manager School official Social service agency official

Next, complete the following statement.

Based on my records or personal knowledge, I believe that one (or both) of the above-named taxpayer(s) **and** (check the box that applies)

- Child 1 Child 2 Child 1 and 2 lived together at the following address:

Address (number and street) ▶ _____

City, town or post office, state, and ZIP code ▶ _____

from month ▶ _____ day ▶ _____, 2003, through month ▶ _____ day ▶ _____, 2003.

Under penalties of perjury, I declare that I have examined this affidavit, and to the best of my knowledge and belief, it is true, correct, and complete.

Third Party Sign Here ▶

Date ▶

Your name (print or type) ▶ _____ Title (if any) ▶ _____

Name of organization (if any) ▶ _____

Address (including city, town or post office, state, and ZIP code)	Your daytime phone number () () () () ()
--	--

Instructions

Purpose of Form

Use Form 8836 if the IRS sent this form to you and you have a qualifying child for the earned income credit (EIC). We need this form to show that you and your child met the **residency test** (defined on this page) for 2003.

Who Must File

File this form **only** if:

- You are claiming or expect to claim the EIC with a qualifying child for 2003 **and**
- The IRS sent this form to you with a letter directing you to file it.

If you do not file Form 8836, the IRS will not allow the EIC with a qualifying child for 2003.

For details on the EIC eligibility rules, including the definition of qualifying child, see **Pub. 596**, Earned Income Credit (EIC). You can order Pub. 596 by calling **1-800-TAX-FORM** (1-800-829-3676) or you can download it from the IRS website at **www.irs.gov**.

Pre-recorded information about the EIC is also available by phone 24 hours a day, 7 days a week. Call **1-800-829-4477** and select TeleTax Topic No. 601. Have paper and a pen or pencil handy to take notes.

When To File

There are two different time periods for filing Form 8836 for 2003. You may file Form 8836 either:

- **Before January 1, 2004.** If you file the form during this period, **you may be able to avoid a delay in receiving the EIC part of your tax refund for 2003.**
- **With your 2003 tax return.** Under this option, the EIC part of your refund **will be delayed** while we review the information you submitted.

Where To File

Send the form to:

**Internal Revenue Service
Stop 4300, Annex R2
Kansas City, MO 64999-0065**

Note. If you file this form after **December 31, 2003**, you may either file it at the above address or attach it to your tax return. If you file it with your return, be sure to send it to the Internal Revenue Service address shown in the instructions for your tax return.



You cannot file **this form** electronically. However, you may still file your tax return electronically. If you do so, send Form 8836 and all required attachments to:

**Internal Revenue Service
Stop 4300, Annex R2
Kansas City, MO 64999-0065**

Residency Test

Your child must have lived with you in the United States for more than half of 2003. Include the time that you or your child are temporarily apart due to a special circumstance, such as military service, school attendance, or juvenile detention. It does not matter where you lived with your child. For example, you may live with your child in a homeless shelter. For more details on the residency test, see Pub. 596.

Special Rule For a Child Who Was Born or Died in 2003. A child is considered to have lived with you for more than half of 2003 if the child was born or died in 2003 **and** your home was the child's home for the entire time he or she was alive in 2003.

What We Will Do After We Receive This Form

We will review the information you send us. We will let you know if you have met the residency test needed to get your EIC. If we need more information, we will contact you.

If you do not meet the residency test for a child, we will let you know. The IRS will not allow the EIC based on that child.

How To Get Help

Call **1-800-294-2723** if you need assistance completing this form or you are having difficulty obtaining the documentation you are required to provide with this form. Assistance is available Monday through Friday from 8:00 a.m. to 8:00 p.m. Eastern time.

You may also visit any IRS Taxpayer Assistance Center. To find out the location and hours of the nearest center, call **1-800-829-1040** or visit the IRS website at **www.irs.gov/localcontacts**. You also can contact the Taxpayer Advocate Service at **1-877-777-4778** or the local Taxpayer Advocate office in your area.

Part I

P.O. Box. Enter your box number **only** if your post office does not deliver mail to your home. Otherwise, enter your home street address.

Daytime and Evening Phone Numbers. Providing your daytime and evening phone numbers may help speed the processing of this form. We may have questions about the information you provided. By answering our questions over the phone, we may be able to continue processing the form without mailing you a letter. If you will be filing a joint return, you may enter either spouse's phone numbers.

Part II

Be sure that any child named is your qualifying child and you expect to claim that child for the EIC on your 2003 tax return.

Your qualifying child must have a valid social security number (SSN), unless the child was born and died in 2003. If the qualifying child was born and died in 2003

and did not have an SSN, attach a copy of that child's birth certificate to Form 8836 and enter "Died" instead of the child's SSN.

For purposes of claiming the EIC, a valid SSN is a number issued by the Social Security Administration unless "Not Valid for Employment" is printed on the social security card and the number was issued solely to apply for or receive a Federally funded benefit.

If you have two qualifying children you may need to complete more than one Form 8836. For example, if in Part IV a doctor is signing for Child 1 and a clergyman is signing for Child 2, you will have to complete two forms. List Child 1 on the form you are giving to the doctor and Child 2 on the form you are giving to the clergyman.

Do not provide information for more than two qualifying children. You need only two qualifying children to claim the maximum EIC.

Part III

You must attach documentation showing that each qualifying child lived with you for more than half of 2003. You may need to send more than one item to show that your child lived with you for more than half of 2003.

If you and your spouse are filing a joint return, you only need to show that one of you lived with your child for more than half of 2003.

Who Can Provide Documents to You. You may submit documentation from any of the following third parties (other than you or your spouse).

- School official (such as a teacher, principal, or administrative assistant).
- Health-care provider (such as your doctor, your nurse practitioner, or a clinic official).
- Member of the clergy (such as your minister, priest, rabbi, or imam).
- Child-care provider who is age 18 or older (and not your neighbor or relative) **or** licensed or regulated by the state or local government for the area in which the child care was provided.
- Your employer.
- Landlord or property manager.
- Social service agency official (such as a case worker at a public assistance office).
- Community-based organization official (such as an official from the YMCA, YWCA, Boy Scouts, Girl Scouts, Boys and Girls Clubs, 4-H, Little League, Police Athletic League, immigrant advocacy groups, low-income taxpayer clinics, neighborhood associations, homeowners and condominium associations and other non-profit groups).
- Indian tribal official.
- Utility company (such as an electric power or natural gas company).

What Kind of Documents You Must Provide. You may provide either of the following from any third party listed above:

- A copy of an official record (such as child-care records, a lease, medical records, a pay stub, or school records), or
- A letter on official letterhead.

You also may ask any third party that is listed in Part IV of the form to complete the Part IV affidavit to show that you and your child lived together for part or all of 2003. See the instructions for Part IV on page 4.

What the Documents Must Show. If you send an official record or letter, it must clearly show:

- Your name, your child's name, or both names, and
- A street address and the dates that you or your child lived at that address during 2003, and
- The name, address, and phone number of the person or organization that provided the record or letter.

If someone fills out Part IV of this form for you, be sure that it is complete.

How Many Documents Do You Need? You may submit any combination of the documents listed above as long as they show, when taken together, that you lived with your child for more than half of 2003. In some cases, a single document will show that you and your child lived at the same address. In other cases, you may need to provide one document showing your name and address as well as a second document showing your child's name with the same address. Multiple documents may be necessary to show that your address and your child's address were the same for more than half of 2003.

Here are a few acceptable combinations of documents:

- One document that shows that both you and your child lived at the same address for more than half of 2003.
- One document that shows that you lived at an address for more than half of 2003 and a second document that shows that your child lived at the same address during the same period of time.
- One document that shows that you and your child lived at the same address for part of 2003 and a second document that shows that you and your child lived together for the remainder of 2003.
- If you have two children, separate documents for each child to show that each one lived with you for more than half of 2003.
- If you have two children, one document to show that both of your children lived with you for more than half of 2003.

Example 1. You attach a letter on official letterhead from Acme Medical Clinic showing that your child lived with you from January 1, 2003, through March 31, 2003. You also have Reverend Smith, your clergyman, complete Part IV showing that you and your child lived together from April 1, 2003, through July 31, 2003. You check the second and third boxes in Part III. Because the total time shown is more than half of the year, the residency test is met.

Example 2. You attach a transcript of your child's grades from the Washington Elementary School showing that your child lived with you from January 1, 2003, through May 31, 2003. You also attach a letter on official letterhead from the principal of the Lincoln Middle School. The letter shows the dates of school attendance and that the child's address was the same as yours. The letter covers the period from September 1, 2003, through October 31, 2003. You check the first two boxes in Part III. Because the total time shown is more than half of the year, the residency test is met.

Note. If you cannot obtain official records, a letter, or a completed Part IV from one or more third parties to show that your child lived with you for more than half of 2003, call **1-800-294-2723** and we will help you.

Signing the Form. You must sign and date Part III under penalties of perjury before you send it to us with the documents. Criminal penalties may be imposed for making a false statement.

Part IV

You may skip Part IV if you are submitting official records or letters that show that your child lived with you for more than half the year in 2003.



If you need to provide more than one affidavit (Part IV) to show that your child lived with you for more than half of 2003, complete as many additional Forms 8836 as you need. On the additional Forms 8836, you do not have to enter your spouse's name and SSN or your address.

Neither you nor your spouse may complete this part. A third party listed in Part IV who has records that show, or who personally knows, that you and your qualifying child lived together for part or all of 2003 must complete this part. The third party must complete all applicable information and sign Part IV under penalties of perjury. If the third party does not complete all applicable information in Part IV, the affidavit may not be accepted. Criminal penalties may be imposed for making a false statement.

Privacy Act and Paperwork Reduction Act Notice.

The Privacy Act of 1974 and the Paperwork Reduction Act of 1980 require that when we ask you for information we must first tell you our legal right to ask for the information, why we are asking for it, and how it will be used. We must also tell you what could happen if we do not receive it and whether your response is voluntary, required to obtain a benefit, or mandatory under the law.

This notice applies to all papers you file with us. It also applies to any questions we need to ask you so we can complete, correct, or process your return; figure your tax; and collect tax, interest, or penalties.

Our legal right to ask for information is Internal Revenue Code sections 6001, 6011, and 6012(a), and their regulations. They say that you must file a return or statement with us for any tax for which you are liable. Your response is mandatory under these sections. Code section 6109 and its regulations say that you must provide your taxpayer identification number on what you file. This is so we know who you are, and can process your return and other papers.

You are not required to provide the information requested on a form that is subject to the Paperwork Reduction Act unless the form displays a valid OMB control number. Books or records relating to a form or its instructions must be retained as long as their contents may become material in the administration of any Internal Revenue law. Generally, tax returns and return information are confidential, as stated in Code section 6103.

We ask for tax return information to carry out the tax laws of the United States. We need it to figure and collect the right amount of tax.

We may give the information to the Department of Justice and to other Federal agencies, as provided by law. We may give it to cities, states, the District of Columbia, and U.S. commonwealths or possessions to carry out their tax laws. We may also disclose this information to other countries under a tax treaty, or to Federal and state agencies to enforce Federal nontax criminal laws and to combat terrorism.

If you do not file a return or give fraudulent information, you may be charged penalties and be subject to criminal prosecution.

Please keep this notice with your records. It may help you if we ask you for other information. If you have any questions about the rules for filing and giving information, please call or visit any Internal Revenue Service office.

The time needed to complete and file this form will vary depending on individual circumstances. The estimated average time is: **Recordkeeping**, 6 min.; **Learning about the law**, 11 min.; **Preparing the form**, 24 min.; **Copying, assembling, and sending the form to the IRS**, 20 min.

If you have comments concerning the accuracy of these time estimates or suggestions for making this form simpler, we would be happy to hear from you. You can write to the Tax Products Coordinating Committee, Western Area Distribution Center, Rancho Cordova, CA 95743-0001. **Do not** send the form to this address. Instead, see **Where To File** on page 2.



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Announcement and Report Concerning Pre-Filing Agreements

Announcement 2003-43

Introduction

This announcement is issued pursuant to the Conference Report to H.R. 4577 (Pub. L. 106-554), *The Community Renewal Tax Relief Act of 2000*, which requires that the Secretary of the Treasury make publicly available an annual report relating to the Pre-Filing Agreement (“PFA”) program operations for the preceding calendar year. The Conference Report states that the report is to include: (1) the number of pre-filing agreements completed, (2) the number of applications received, (3) the number of applications withdrawn, (4) the types of issues which are resolved by completed agreements, (5) whether the program is being utilized by taxpayers who were previously subject to audit, (6) the average length of time required to complete an agreement, (7) the number, if any, and subject of technical advice and Chief Counsel advice memoranda issued to address issues arising in connection with any pre-filing agreement, (8) any model agreements, and (9) any other information the Secretary deems appropriate. This is the third annual report. It provides information concerning activity under the permanent PFA program (Rev. Proc. 2001-22, 2001-1 C.B. 745), during calendar year 2002.

Background

The Large and Mid-Size Business Division (“LMSB”) within the Internal Revenue Service serves corporations and partnerships with assets greater than \$10 million. In 2002, approximately 150,000 corporations and partnerships filed returns reporting assets in this range. The returns filed by these taxpayers present a wide variety of complex issues. The largest of these taxpayers deal with the IRS on a continuous basis.

One of LMSB’s strategic initiatives is issue management. Through effective issue management, LMSB seeks to resolve issues of tax controversy on a more current basis. This includes, but is not limited to, increasing the efficiency of the examination process and seeking alternative issue resolution tools. The Pre-Filing Agreement program was designed to support

LMSB’s issue management strategy. LMSB believes the Pre-Filing Agreement program reduces taxpayer burden and makes more effective use of IRS resources by resolving or eliminating tax controversy before the tax return is filed.

The PFA program is designed to permit a taxpayer to resolve, before the filing of a return, the treatment of an issue that otherwise would likely be disputed in a post-filing examination. The PFA program is intended to produce agreement on factual issues and apply settled legal principles to those facts. A PFA is a specific matter closing agreement under § 7121 of the Internal Revenue Code and resolves the subject of the PFA for a specified taxable period. Execution of a PFA that resolves issues prior to filing permits taxpayers to avoid costs, burdens and delays that are frequently incident to post-filing examination disputes between taxpayers and the IRS.

PFA Program

As a result of the success of a pilot program, the IRS established a permanent PFA Program with the issuance of Rev. Proc. 2001-22. Although many of the procedures remained the same, there were some significant changes, including:

1. All taxpayers, both Coordinated Issue and Industry cases, within the jurisdiction of LMSB are eligible to participate;
2. More issues are considered appropriate;
3. There are fewer excludible circumstances;
4. Certain international issues are now considered appropriate; and
5. A user fee was implemented for those taxpayers accepted into the program.

PFA Process

The PFA process is managed and conducted by LMSB Industry Directors and field staff, with support from the Office of Pre-Filing and Technical Guidance in LMSB Headquarters. The PFA Program Manager receives all applications and, with the assistance of the Technical Advisors and the Office of Chief Counsel, ensures that the issues presented are appropriate for inclusion in the PFA program.

The Industry Director with jurisdiction over the taxpayer makes the final deci-

sion whether to accept a taxpayer’s request for participation in the PFA program. The criteria for selecting a request include:

- a. The suitability of the issue presented by the taxpayer;
- b. The direct or indirect impact of a PFA upon other years, issues, taxpayers, or related cases;
- c. The availability of IRS resources;
- d. The ability and willingness of the taxpayer to dedicate sufficient resources to the process;
- e. The likelihood that the PFA may result in contrary positions with respect to an item or transaction (“whipsaw”); and
- f. The probability of completing the examination of the issue and entering into a PFA by the target date.

For the cases selected, a mandatory orientation session for the examination team and the taxpayer is conducted. Subsequently, the taxpayer and examination team convene a joint planning meeting to reach agreement on a proposed timeframe, to identify and arrange for IRS access to relevant records and testimony, and to define the potential scope and nature of the PFA.

The examination team conducts the factual determination and issue development consistent with IRS auditing standards. Based upon an examination of the issue, the Team Manager prepares a PFA recommendation for the Industry Director. The Industry Director’s decision to execute a PFA Closing Agreement is based on the Team Manager’s recommendation and discussions with the PFA Program Manager, Chief Counsel attorneys, appropriate Technical Advisors and the taxpayer. Following Chief Counsel review to ensure that the proposed PFA conforms with guidance provided in Rev. Proc. 68-16 (regarding closing agreements), the Industry Director could execute a PFA if he or she determines that:

- a. Entering into the PFA is consistent with the goals of the PFA program as stated in Rev. Proc. 2001-22;
- b. The resolution in the PFA reflects settled legal principles and correctly applies those principles (or positions authorized under Delegation Order Nos. 236 or 247) to facts found by the examination team; and
- c. There appears to be an advantage in having the issue(s) permanently and conclusively closed for the taxable period covered by the PFA, or that the taxpayer shows

good and sufficient reasons for desiring a closing agreement and that the United States would sustain no disadvantage through consummation of such an agreement (see § 301.7121-1(a) of the Procedure and Administration Regulations).

Program Oversight

A designated PFA Program Manager assigned to the Office of Pre-Filing and Technical Guidance in LMSB Headquarters provides oversight for the PFA program. The PFA Program Manager provides assistance to taxpayers, Industry Directors and Team Managers throughout the process.

Pre-Filing Agreement Program Accomplishments

Statistical Overview of PFA Program — Calendar Year 2002

The table below reflects activity concerning those PFA requests which were received in calendar year 2001 and carried over into calendar year 2002.

Overview of PFA Applications Received in Calendar Year 2001	Totals
Applications Pending Acceptance/Rejection on January 1, 2002	5
Applications In-Process on January 1, 2002	7
Applications Rejected in 2002	1
Applications Withdrawn in 2002	0
Applications for Which There Were Closing Agreements in 2002	7
Applications Pending Acceptance/Rejection on December 31, 2002	0
Applications in-Process on December 31, 2002	4

The table below reflects the status of PFA requests received in calendar year 2002.

Overview of PFA Applications Received in Calendar Year 2002	Totals
Applications Received in 2002	44
Applications Accepted in 2002	25
Applications Rejected in 2002	14
Applications Withdrawn before Acceptance/Rejection in 2002	1
Applications Withdrawn after Acceptance in 2002	4
Applications for Which There Were Closing Agreements in 2002	5
Applications Pending Acceptance/Rejection on December 31, 2002	4
Applications in-Process on December 31, 2002	16

Description of Applications Received in Calendar Year 2002

The forty-four applications that were received for the PFA program in calendar year 2002 came from each LMSB industry segment and involved a variety of issues.

Number of Requests Received and Accepted by Industry Segment

<i>Industry Segment</i>	<i>Received</i>	<i>Accepted</i>
Financial Services (FS)	6	3
Retailers, Food, Pharmaceuticals & Healthcare (RFP&H)	9	5
Natural Resources & Construction (NR&C)	16	9
Communications, Technology & Media (CT&M)	6	4
Heavy Manufacturing & Transportation (HM&T)	7	4
Total	44	25

Types of Issues Received

Issue	Received
Original Issue Discount Issue Price	1
Fair Market Value of Assets Exchanged for Stock	2
Abandonment Loss	1
Sale of Assets – Amount of Built-in Gains and Built-in Losses	1
Sale of Assets &/or Stock	2
Allocation of Sales Price	1
Research & Experiment Credit	5
Sale – Leaseback	1
Bad Debts &/or Worthless Securities	3
Legal/Consulting Fees vs Lobbying	1
Bank Owned Life Insurance	1
Spin-off & Merger	1
Deduction for Dividends Paid to Employee Stock Ownership Plan	1
Investigatory Costs	3
Allocation of Losses	1
Restructuring	1
Period of Income Inclusion	1
Tax Motivated Transaction	2
Donation of Intangibles	2
Donation of Real Property	1
Qualified Conservation Donation	1
Liquidation	2
Synthetic Fuel Credit	9
Total	44

Reasons Why Applications Received in Calendar Year 2002 Were Not Accepted

Fourteen of the applications received in 2002 were not considered appropriate for the PFA program.

Reasons for Non-acceptance	Applications
Issue Not Suitable or Ineligible	6
International Issue Not Listed in Rev. Proc. 2001–22	2
Not Well-Settled Law	4
Tax Motivated Transaction	2
Total	14

Taxpayer Withdrawal (3)

In accordance with the procedures set forth in Section 8 of Rev. Proc. 2001–22, three taxpayers withdrew from the PFA process — 2 after their requests had been accepted and one prior to acceptance. In two cases, the withdrawals were necessitated, as indicated by the taxpayers, by their inability to devote sufficient resources required to successfully continue the PFA process. In the other instance, the taxpayer withdrew because of the reluctance of the Industry Director to reach agreement on all the issues in the taxpayer’s application.

IRS Withdrawal (2)

The Service withdrew from the PFA process in one case where, after significant factual development and legal analysis of all of the issues, the Service concluded that the issues did not involve well settled law. The Service withdrew from the PFA process in a second case where, after factual development, the Service determined that the issues were not suitable for the PFA program and would be more effectively considered during a post-filing examination.

PFA’s Executed (12)

Twelve PFA’s were completed in calendar year 2002, resulting in the execution of closing agreements.

The Office of Chief Counsel provided advice to the examination teams and assisted in the drafting and review of the PFA closing agreements. No Technical Advice or Chief Counsel Advice Memoranda were issued for issues addressed in the PFA process. The executed PFA’s covered the following issues:

PFA's Executed by Issue

Year Application Received	Issue	Number
2001	Tax Basis/Holding Period/Reorganization	1
2001	Bad Debts & Worthless Stock	1
2001	Accounting Method	1
2001	Reorganization & Basis of Stock	1
2001	Donation of Intangibles	2
2001	Gain on Sale of Assets	1
2002	Treatment of costs associated with acquiring another corporation	1
2002	Allocation of Sales Price	1
2002	Sale of Assets – Amount of Built-in Gains and Built-in Losses	1
2002	Spin-off & Merger	1
2002	Deduction for Dividends Paid to ESOP	1
	Total	12

Tax Basis/Holding Period/Reorganization

The taxpayer requested a determination concerning the tax basis and holding period of stock acquired in a reorganization described in §§ 368(a)(1)(B) and 368(a)(2)(E). The parties entered into a closing agreement that established the amount of the taxpayer's basis in the stock. The closing agreement also established the date that the taxpayer will have met the five-year holding period prescribed by § 355(d).

Bad Debts & Worthless Stock

The taxpayer and the IRS entered into a closing agreement stipulating that the entire debt owed by a subsidiary to the taxpayer had become worthless within the meaning of § 166(a)(1) during the taxpayer's taxable year ending in 2002. In addition, the closing agreement stipulated that the taxpayer's securities in the subsidiary had become worthless within the meaning of § 165(g)(3) during the taxpayer's taxable year ending in 2002.

Accounting Method

The taxpayer requested a determination concerning the proper tax accounting treatment of rebates paid to customers. The taxpayer had acquired all the assets and liabilities of another corporation that used a different method of accounting for rebates than the taxpayer. In integrating the two accounting systems, the taxpayer wanted to use the method previously used by the ac-

quired corporation. A closing agreement was executed allowing the taxpayer to use the desired method of accounting.

Reorganization & Basis of Stock

The taxpayer requested a determination concerning its basis in stock acquired in a reorganization described in § 368(a)(2)(E). The parties entered into a closing agreement whereby it was agreed that the taxpayer could determine its basis under § 1.358-6 as if the basis in the acquired stock was determined under § 362(b). In addition, the parties agreed to the amount of the basis.

Donation of Intangibles (2)

In each of these unrelated cases, taxpayers sought an agreement as to the fair market value of certain intellectual property donated to qualified organizations. In both instances, a closing agreement was reached specifying the fair market value of the property contributed. The closing agreement did not address the deductibility of the charitable contributions.

Gain on Sale of Assets

In this case, the taxpayer sold assets to an unrelated third party in a transaction described in § 1060. The purchaser paid cash and assumed liabilities in exchange for the assets. A closing agreement was executed establishing the amount of capital gain and ordinary loss to be reported from the transaction for each asset class under § 1060.

Treatment of Costs Associated with Acquiring another Corporation

Taxpayer requested a determination with respect to the treatment of certain costs associated with the acquisition of another corporation. A closing agreement was executed specifying, based on the facts, the amount deductible as ordinary and necessary business expenses under § 162, the amount allowable under § 195 as start-up expenditures and the amount required to be capitalized under § 263.

Allocation of Sales Price

In this case, the taxpayer sold assets to a third party. The taxpayer requested an agreement concerning the proper allocation of the sale proceeds among the assets sold. A factual determination was reached concerning the allocation of the sales proceeds and the amount and character of income, gain and loss to be reported.

Sale of Assets — Amount of Built-in Gains and Built-in Losses

The taxpayer requested a factual determination regarding the amount of built-in gains and built-in losses, as defined in §§ 1374(d)(3) and (d)(4), recognized from the sale of its qualified subchapter S subsidiaries (QSubs). Under § 1.1361-5, the sale of the QSubs was treated as a direct sale of the assets of the QSubs. The examination consisted of a review of the taxpayer's computations and a review of the

books and records and other information provided by the taxpayer. A closing agreement was entered into specifying the amounts of gain and loss to be recognized.

Spin-off & Merger

The taxpayer distributed all of the issued and outstanding stock of a number of its wholly-owned subsidiaries to shareholders in complete redemption of their shares. Subsequent to the distribution, the subsidiaries merged into another corporation. An agreement was reached indicating the distribution satisfied the requirements of § 355, other than the business purpose requirement (which was not addressed by the closing agreement), and therefore, subject to satisfying the business purpose requirement, no gain or loss was recognized by any of the shareholders or any of the corporations as a result of the distribution and subsequent merger.

Deduction for Dividends Paid to ESOP

The taxpayer requested a determination regarding the treatment of dividends that were paid by the taxpayer to an Employee Stock Ownership Plan (ESOP) and were subject to a distribution/reinvestment election during the first 90 days of 2002. A closing agreement was executed stipulating the amount of dividends that qualified as applicable dividends under § 404(k) and therefore were deductible by the taxpayer.

Closing Agreements

A pro forma or model agreement does not exist for a PFA Closing Agreement. A PFA represents a specific matter closing agreement under § 7121. The closing agreements entered into under this program were prepared with assistance from the Office of Chief Counsel and conform to the guidance provided in Rev. Proc. 68-16.

PFA Program Utilization

The PFA Program is available to all taxpayers under the jurisdiction of LMSB. During calendar year 2002, 44 taxpayers submitted PFA requests. These included both Coordinated Industry Case (CIC) taxpayers that are typically subject to examination on a continuing basis and Industry Case (IC) taxpayers that are subject to examination on a more limited basis. Of the 44 requests, 38 were from CIC taxpayers and 6 from IC taxpayers. For the twelve cases that resulted in closing agreements during calendar year 2002, 10 were with CIC taxpayers and 2 were with IC taxpayers.

Processing Statistics

The average elapsed time to resolve the 12 cases that resulted in closing agreements in calendar year 2002 (the applications of which were received in 2001 and 2002) and the 5 cases that were withdrawn in calendar year 2002 was 199.1 days.

Average Processing Time for Seventeen Cases Closed in 2002	Range (Elapsed Days)	Average (Elapsed Days)
Phase I – Application Screening Process	23–92	53.1
Phase II – PFA Evaluation Process	8–320	146.1
Total Time to Close a PFA Case	54–392	199.1

Phase I – Application Screening Process

Phase I is the screening process to determine if an application is appropriate for inclusion in the PFA program. This screening process includes obtaining comments from various LMSB functions and Chief Counsel, the review of these comments and the acceptance/rejection of an application by the Industry Director. Of the 44 applications received during the calendar year 2002, 39 completed the Phase I Process. For these 39 applications, the average time from the date an application was received by the IRS until the Industry Director rendered a decision to accept or reject an application

was 65 days. For the 12 cases that resulted in closing agreements in 2002, the average time for Phase I was 52.8 days.

Phase II – PFA Evaluation Process

The second (and final) phase in the PFA program process was the evaluation phase. This phase began when the Industry Director accepted an application into the PFA program and ended when a PFA closing agreement was executed or the process ended in a withdrawal. The average elapsed time for the 12 cases that resulted in closing agreements and the 5 cases that were withdrawn in calendar year 2002 was 146.1 days.

Program Evaluation

The PFA Program Manager ensures that an evaluation of all of the PFA program cases, based on feedback from LMSB employees and taxpayer participants, is solicited. As a part of this program evaluation, LMSB and taxpayer participants were asked to provide the direct examination time expended to complete the PFA and an estimate of the direct examination time it would have taken to resolve the issue in a post-filing context. The table below indicates the results for those that responded to the solicitation:

Cumulative Hours (Executed PFAs)	Taxpayer (Hours)	LMSB (Hours)
Actual – PFA Process	3,984	8,166
Estimated – Post-Filing Process	6,300	10,407
Estimated Savings	2,316	2,241
Estimated Savings Percentage (Average)	36.8%	21.5%

Cumulative Hours (Executed PFAs)	Taxpayer (Hours)	LMSB (Hours)
Estimated Savings Percentage (Range)	21.4%–85%	(4.8)%–51.2%

Comparative Analysis — Processing Statistics

The average total time to conclude the 12 cases that resulted in closing agreements in calendar year 2002 was 235.4

days. The range was from 151 to 392 days. Illustrated below are the average elapsed time (in days) processing statistics for the 12 cases that resulted in closing agreements in calendar year 2002, the 7 cases that resulted in closing agreements in cal-

endar year 2001, and the 11 cases that resulted in closing agreements under the pilot program.

Average Processing Time for PFAs (Days)	Overall Pilot (11 cases)	Program CY 2001 (7 cases)	Program CY 2003 (12 cases)
Phase I – Application Screening Process	38.3	46.6	52.8
Phase II – PFA Evaluation Process	242.2	126.1	182.6
Total Time to Complete a PFA	280.5	172.7	235.4

The increased processing time for 2002 can be attributed to the degree of complexity of the issues and the time necessary to develop the factual aspects of the issues. Generally, the more complex and examination intensive the issue is, the greater the time necessary to complete the process.

Pre-Filing Agreement Program Summary

The PFA program is now available to all LMSB taxpayers, including taxpayers that are not currently under examination. While the PFA program will continue to be limited to issues that involve settled legal principles, the list of recommended issues has been expanded, and now includes certain international issues. Generally, the operational procedures used during the PFA pilot program were adopted and enhanced in the permanent PFA program.

Overall, the PFA program is meeting the LMSB strategic program objectives as contained in its issue management strategic ini-

tiative. Issues of potential controversy are being resolved more efficiently and on a more current basis yielding benefits to taxpayers and the IRS.

The principal author of this announcement is J. Michael Mann, in the Office of Pre-Filing and Technical Guidance, Large and Mid-Size Business Division. For further information regarding this announcement, contact Mr. Mann at (202) 283–8424 (not a toll-free call).

Correction to Rev. Rul. 2003–50 — BLS Department Store Indexes for March 2003

Announcement 2003–44

PURPOSE

This announcement corrects a typographical error in Rev. Rul. 2003–50, 2003–21 I.R.B. 944, Bureau of Labor Sta-

tistics, Department Store Inventory Price Indexes by Department Groups for March 2003. Line 14 (Notions), Column 2 (March 2003), incorrectly reads “797.7.” The correct figure is 797.1.

EFFECTIVE DATE

This announcement is effective for taxable years ended on, or with reference to, March 31, 2003.

EFFECT ON OTHER DOCUMENTS

Rev. Rul. 2003–50 is modified.

DRAFTING INFORMATION

The principal author of this announcement is Michael Burkom of the Office of Associate Chief Counsel (Income Tax & Accounting). For further information regarding this announcement, contact Mr. Burkom at (202) 622–7718 (not a toll-free number).

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified*, below).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it

applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1986 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the

new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified* and *superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case, the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.

E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign Corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.

PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statements of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

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